

STATE OF CALIFORNIA
COMMISSION ON THE 21st CENTURY ECONOMY



STATE OF CALIFORNIA
REVENUE & TAXATION

PUBLIC MEETING

Thursday, September 10, 2009
11:00 a.m. – 6:00 p.m.

University of California, Los Angeles
James West Alumni Center
Collins Alumni Conference Center
325 Westwood Plaza
Los Angeles, California



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A P P E A R A N C E S

COMMISSION ON THE 21ST CENTURY ECONOMY

Commissioners Present

GERRY PARSKY
Commission Chair
Aurora Capital Group

RUBEN BARRALES
President/CEO
San Diego Regional Chamber of Commerce

MICHAEL BOSKIN
Professor
Stanford University

JOHN COGAN
Professor
Stanford University

EDWARD DE LA ROSA
Founder and President
Edward J. De La Rosa & Company, Inc.

CHRISTOPHER EDLEY, JR.
Dean/Professor of Law
Boalt Hall School of Law

WILLIAM HAUCK
Trustee, California State University
Director
Blue Shield of California & Blue Shield Foundation

JENNIFER ITO
Research, Training, Policy Director
SCOPE

FRED KEELEY
Treasurer, County of Santa Cruz
Professor, San José State University

MONICA LOZANO
Publisher/CEO
La Opinión

A P P E A R A N C E S

COMMISSION ON THE 21ST CENTURY ECONOMY

Commissioners Present

Continued

REBECCA MORGAN
President
Morgan Family Foundation
(*Appearing telephonically*)

RICHARD POMP
Alva P. Loisel Professor of Law
University of Connecticut

CURT PRINGLE
Mayor
City of Anaheim

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COTCE Staff Present

MICHAEL C. GENEST
Commission Executive Director
Director of Finance

MARK IBELE
Commission Staff Director
Board of Equalization

ASHLEY SNEE GIOVANNETTONE

LORI HSU

ANTONIO LOCKETT

JESSICA MAR

MICHELLE QUINN
Staff Writer

PHIL SPILBERG
Chief, Financial Research
Department of Finance

MARGIE RAMIREZ WALKER

A P P E A R A N C E S

Tax Advisors

JUNE SUMMERS HAAS
Partner
Honigman Miller Schwartz & Cohn LLP
(*Appearing telephonically*)

CARL JOSEPH
Director
Multistate Taxation Bureau
Legal Division
Franchise Tax Board

PATRICK KUSIAK
Franchise Tax Board

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Public Testimony

GUS KHOURI
California Transit Association

CARL MOREHOUSE
City Council
City of Ventura
and
Southern California Association of
Governments (SCAG)

CHRIS NORBY
Southern California Association of
Governments (SCAG)

MICHAEL D. SHAW
Legislator Director
National Federation of Independent Business

WILLIAM SPILLANE
California State Director
FairTax.org

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A P P E A R A N C E S

Presenters

JOHN BOESEL
President and CEO
CALSTART

WILLIAM G. DOREY
President and CEO
Granite Construction, Inc.

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1 BE IT REMEMBERED that on Thursday,
2 September 10, 2009, commencing at the hour of
3 11:10 a.m., at the University of California, Los
4 Angeles, James West Alumni Center, Collins Alumni
5 Conference Center, 325 Westwood Plaza, Los Angeles,
6 California, before me, DANIEL P. FELDHAUS, CSR 6949,
7 RDR, CRR, in the state of California, the following
8 proceedings were held:

9 *(Commissioner Morgan and Ms. Haas appeared*
10 *telephonically for the meeting.)*

11 CHAIR PARSKY: Becky, are you on?

12 COMMISSIONER MORGAN: Yes, I am.

13 CHAIR PARSKY: And, June?

14 MS. HAAS: Yes, I am.

15 CHAIR PARSKY: Ladies and gentlemen, I'd like
16 to get started with our public meeting on the Commission
17 on the 21st Century Economy.

18 We have on the telephone Becky Morgan, who is a
19 commissioner. We also have June Haas, who has been a
20 former commissioner in Michigan, a tax commissioner in
21 Michigan, a lawyer that has been assisting us in
22 evaluating the potential business net-receipts tax.

23 I know that Ruben Barrales and Curt Pringle
24 will both be here, and they will be joining us shortly.

25 I think all the commissioners have in their book

1 an agenda and a number of supporting documents. And we
2 will have a public comment period. I haven't collected
3 all those that wish to make public comment; and so we'll
4 delay starting the public comment until a little bit
5 later.

6 I just want to make a couple of introductory
7 comments and then talk a little bit about the structure
8 for this session.

9 As I think all of you know, this Commission was
10 formed by the legislative leadership and the Governor to
11 make recommendations with respect to reform of our tax
12 system in California.

13 I think I've mentioned at every public meeting
14 that we have held, the overall objectives are goals that
15 we have been requested to keep in mind and test against
16 the recommendations that we will make.

17 And just to remind people, those included the
18 goal of helping to stabilize state revenues and reduce
19 volatility.

20 Second, to promote long-term economic growth and
21 job creation for the state and its citizens.

22 Third, to establish a tax structure that fits
23 with the state's 21st century economy.

24 Fourth, to improve California's ability to
25 successfully compete with other states and nations for

1 jobs and investment.

2 Fifth, that the recommendation should reflect
3 principles of sound tax policy, including simplicity,
4 competitiveness, predictability, and ease of compliance
5 and administration.

6 And finally, to ensure that the recommendations
7 help the tax structure be fair and equitable to its
8 citizens.

9 Those goals haven't changed from the time we
10 first began. And I want to thank all of the commissioners
11 for the kind of time and effort everyone has put in to
12 try and to come up with a consensus series of
13 recommendations to try to achieve those goals.

14 This subject, I think everyone now, if they
15 didn't at the time we began, realize is a very complicated
16 and difficult subject to deal with and, in particular, a
17 difficult subject to deal with to achieve those goals.

18 Nevertheless, I think it's an incredibly
19 important subject. And I think during the course of
20 this Commission effort, we've seen the difficulties that
21 exist within the state and for the policy leaders or
22 makers in this state with dealing with the revenue side
23 of the California system. And many of the benefits that
24 rightfully should be provided or promised to be provided
25 to our citizens have not been able to be provided because

1 of the fact that the revenues haven't been there in order
2 to accomplish those objectives. And it's created
3 significant harm to our citizens.

4 And so I think the effort at the beginning was
5 important, but it's taken on even more importance, as
6 we've seen what can happen. Hopefully, this economic
7 recession won't be repeated. But business cycles happen.
8 And we've seen what can happen under our current system
9 if, in fact, you have a deep recession, which we have all
10 been experiencing: The amount of unemployment that exists
11 and the failure, if you will, on the part of the revenue
12 base to satisfy the objectives and desires of the
13 legislative body.

14 And so the efforts that this Commission is
15 undertaking, as I said, I think has been important from
16 the beginning. It takes on even more importance. And I
17 think a number of us have indicated the importance of
18 trying to come up with real reform; for reform that needs
19 to be looked at carefully, that needs to be looked at
20 over a period of time.

21 And in that connection, I would say that our
22 job is not to take the place of the Legislature. The
23 Legislature has continuing responsibility to enact laws
24 for California. The Governor obviously has a critical
25 role in that process. But I do think that we were asked

1 to provide specific reforms in connection with that,
2 recognizing that the legislative process will take our
3 reforms and will have to go through their normal
4 committee process, their normal evaluation; and that
5 although there has been an indication between the Governor
6 and the legislative leaders, that there is an expectation
7 for whatever reform proposals are recommended, that there
8 will be a vote on them.

9 I don't think any of the commissioners that I --
10 and I've talked to everyone -- expects that the reform
11 recommendations will be just taken as is.

12 *(Commissioner Barrales entered the meeting*
13 *room.)*

14 CHAIR PARSKY: And especially if we continue
15 to contemplate a brand-new form of tax. That, as you
16 will hear this morning, a lot of work has been done on,
17 but that is very complicated and, not having been in
18 existence, needs careful analytical consideration beyond
19 what this commission could possibly have done in the time
20 frame and with the staff that we have.

21 Despite that, I think you will see very
22 extensive, specific proposals for consideration. And
23 we'll talk more about that.

24 The final thing I want to remind the
25 Commissioners and the public, at the last meeting we

1 came together and agreed on a structure for our
2 recommendations. And this has been posted and it has
3 been discussed. But as we enter into this meeting, I want
4 to remind people of that structure and see if, in our
5 discussions today, we can fit all of the recommendations
6 and desires of commissioners into that structure because
7 we agreed that's the way in which we would proceed.

8 Two basic pieces of material: The
9 recommendations we agreed would fall into three sections.

10 Section 1, the recommendations of statutory
11 tax-law changes, revenue-related, that can be acted on by
12 the State Legislature immediately, and hopefully endorsed
13 unanimously by the Commissioners.

14 Section 2, recommendations of tax-law changes,
15 revenue-related, that can be enacted by changes in the
16 State Constitution or by the State initiative process, and
17 hopefully are endorsed unanimously by the Commissioners.

18 Section 3, the Commission, hopefully
19 unanimously, but with some clear desire on the part of
20 the Commissioners, to maintain great flexibility, to
21 identify areas of reform, whether they be revenue or
22 non-revenue-related that, in commissioners' views, need
23 to be considered by others outside the context of the
24 Commission in order to achieve comprehensive fiscal
25 reform.

1 That will make up the recommendations that we
2 will hopefully come together to make.

3 Then in addition to that, we agreed on a tax
4 package, in general terms, that would make up sections --
5 at least Sections 1 and 2 of the recommendations -- a
6 package, at least at our last session. And that package
7 would include recommendations relating to the personal
8 income tax and, around that, a simplified rate
9 structure -- two potential rates -- a standard deduction,
10 itemized deductions for mortgage interest, charitable
11 giving, and property taxes.

12 However, the commissioners made it clear at the
13 last meeting that a condition to this proposal, or the
14 part of the proposal that deals with the personal income
15 tax, that all AGI brackets, as shown in our last
16 presentation, would need to receive a reduction in taxes
17 in order to endorse a recommendation surrounding the
18 personal income tax.

19 And if that objective cannot be achieved under
20 the two-rate structure, then consideration would be given
21 to other alternative structures.

22 So a condition to the recommendations you will
23 hear relating to the personal income tax was that all AGI
24 brackets would need to receive a reduction. And there is
25 heightened sensitivity on behalf of many, if not most, of

1 the Commissioners, to make sure we are cognizant of the
2 distribution impact of changes like that. And that
3 although I think there is a belief that if there is a
4 way to reduce the overall general fund on the dependence
5 on the personal income, that's an objective that we
6 potentially could rally around, but not if it means that
7 the higher-income groups were going to get a reduction at
8 the expense of the middle- or lower-income groups getting
9 an increase.

10 Second, the corporate tax under this tax package
11 as identified, would be eliminated; that a business
12 net-receipts tax, as previously outlined, would be
13 established; and that the general fund sales tax, a
14 portion of the sales tax going to the general fund, would
15 also be eliminated.

16 There was a note that Commissioners agreed to,
17 that if we do not recommend the business net-receipts tax,
18 we would consider a recommendation to extend the state
19 general sales tax to services. That was outlined also
20 as part of the package.

21 In addition, as part of the package and
22 potentially inclusion in Sections 1 or 2, a pollution
23 tax on carbon-based fuels, a split-roll property tax for
24 non-residential property, a royalty on expanded oil
25 drilling, the establishment of a reserve or rainy-day

1 fund, with a note also that the recommendation would
2 include a dedication of these funds to the general fund
3 only.

4 And finally, the potential establishment of a
5 new tax dispute resolution forum.

6 That tax package was agreed to by the Commission
7 as the structure that we would attempt to coalesce around
8 in terms of our recommendations for Sections 1 and 2.

9 Section 3 could include more than was embodied
10 in that tax package. And if we couldn't reach consensus
11 around any one of the -- all of the elements outlined,
12 then that element could also be included in Section 3.
13 And we will discuss that as we go through here.

14 But I think I've accurately reflected what
15 we had agreed the approach we would take to our
16 recommendation section. And we have heard from a number
17 of commissioners about items that they are particularly
18 interested in as part of reform outside of this package,
19 as described. And we will air those, discuss those, as
20 we proceed with this meeting.

21 The only other thing I would say before we go
22 through these elements, is that we said at the last
23 meeting that given the potential for several new taxes --
24 the business net-receipts tax and the pollution tax --
25 that we felt that further work, extensive work needed to

1 be done with respect to both of those.

2 And I want to thank individual commissioners
3 Chris Edley and John Cogan, with respect to the business
4 net-receipts tax, and Fred Keeley with respect to the
5 pollution tax. That these commissioners helped
6 extensively in preparing for this meeting in connection
7 with those two possible recommendations.

8 With respect to the business net-receipts tax,
9 we held a planning session which both commissioners
10 participated in, and which staff -- not only our staff,
11 but staff from the Franchise Tax Board, staff from the
12 Board of Equalization, and individual staffs from the
13 legislative leaders -- participated in planning for
14 two public workshops on this new and quite complicated
15 potential tax. And then we conducted public workshops,
16 hearing from a variety of interested parties, affected
17 parties. And several commissioners attended those
18 workshops: Bill Hauck, Jennifer Ito, Edward De La Rosa,
19 Ruben Barrales attended those workshops, as everyone was
20 welcome to. And I thank all of you for doing that.

21 I also want to thank all the other commissioners
22 for the input that you have given extensive e-mails from
23 all the commissioners in connection with their thoughts
24 and ideas around this.

25 That gives you, by way of background, the kind

1 of effort that has been undertaken. And you will see,
2 posted on the Web site, the results of that effort with
3 respect to this entire package.

4 And, as I said, several commissioners have
5 indicated a desire to consider other recommendations; and
6 we will discuss each of those in connection with this
7 meeting today.

8 Finally, we have scheduled another meeting, as
9 needed, on Monday at Berkeley. Not without some level of
10 influence from our Dean of the Boalt Law School. But we
11 do have one scheduled. And my only concern about that
12 is, I know that several commissioners are unable to
13 attend that meeting. We will certainly give them access
14 by phone, as we have Becky Morgan today. But we will
15 need to address the fact that several commissioners can't
16 attend that meeting.

17 My advice would be, let's see where we are as
18 we get through today's meeting, and see what is needed
19 between now and Monday.

20 And then we have a deadline of submitting our
21 final report on September 20th. And the Governor has
22 indicated that he would like to call a special session
23 of the Legislature to consider the recommendations.

24 Inherent in that, is a full, extensive
25 legislative session, including extensive hearings and

1 extensive additional analysis of all elements of any
2 recommendation that we would make.

3 COMMISSIONER EDLEY: Spell-checking.

4 CHAIR PARSKY: The dean said "Spell-checking."
5 Yes, I think that's true.

6 So with that framework, what I'd like to suggest
7 is that we work our way through this package. And my
8 suggestion to begin, would be to turn the discussion over
9 to, first, John Cogan and Chris Edley, who have been
10 extensively involved in the analytical framework for the
11 potential business net-receipts tax.

12 But before I do that, I just want to acknowledge
13 and thank several members of our staff, because they have
14 worked around the clock in an effort to put this material
15 together.

16 I think all of you know Mike Genest, Mark Ibele,
17 and Phil Spilberg. All three of these people, all of
18 whom have worked tirelessly to try to pull together a
19 very, very complicated subject.

20 I also want to give special thanks to Bob Cline
21 of Ernst & Young, who has worked also extensively with us
22 in connection with the business net-receipts tax.

23 Special thanks go to a number of members of
24 the Franchise Tax Board. Carl Joseph, Pat Kusiak, Doug
25 Powers, and Andrea Chang, all of whom tirelessly worked

1 to pull together extensive legislative language that has
2 all been posted on our Web site, is available to all the
3 commissioners with respect to these potential changes.

4 And Pat Landingham -- is that the right way to
5 pronounce it? -- has done an incredible amount of work
6 for us in trying to give as accurate a projection of
7 revenues coming forward.

8 I can't express enough the kind of voluntary
9 efforts put in by these people.

10 So with that, I'd like to turn this over to
11 John and Chris.

12 At the end of this presentation on these
13 elements of the package, all commissioners can ask
14 questions, then maybe we'll take a break, and then we
15 will come back and let commissioners express their views
16 on this element.

17 COMMISSIONER EDLEY: And then what about the
18 proposals?

19 CHAIR PARSKY: Then each of the other pieces
20 will be presented in the same context, with questions,
21 and then come back and make comments. So we'll treat
22 each element of the package the same, and we'll try to
23 get through this in the time frame allowed.

24 COMMISSIONER COGAN: Gerry, thank you very
25 much.

1 Commissioners, Chris and I have been working
2 for the last month, as Gerry said. We tried to put
3 together a package that we hoped would be able to achieve
4 a unanimous recommendation by the Commission.

5 We've divided up the presentation of our work.
6 It was divided by the flip of a coin. I won, Gerry lost;
7 and so I get to talk about the tax cuts, and then Chris
8 gets to talk about the tax increases.

9 But in going through this process, I have to say
10 that I've discovered why I'm not a legislator. Writing
11 tax policy is extraordinarily, extraordinarily difficult.
12 And as I think you'll see, in many ways, some arbitrary
13 decisions have been made, but they're unavoidable.

14 But let me begin by emphasizing a point that
15 Chris and I mentioned in our memo to you all, and that is
16 that we're confident that this general approach that we
17 are proposing is a good policy for California's economy.
18 But the magnitude of the change that we are considering
19 is so large, I don't think there's ever been a change
20 proposed for California this large in its history, that
21 we don't believe that we should be recommending an
22 up-or-down vote by the Legislature at this juncture.

23 What we need to have is a process by which the
24 ramifications of the proposal are fully vetted and all
25 the provisions of a new business tax for California have

1 been fully considered.

2 And so what we're recommending to the Commission
3 is that you consider this to be a proposal for further
4 inquiry. That is, we believe that the proposal, as
5 offered, warrants your serious consideration and your
6 recommendation. But the recommendation is really to move
7 the process forward at the Legislature. We think this
8 approach is very, very promising, but we realize that it
9 needs a lot more vetting before it's ready for a vote by
10 the Legislature.

11 So with that in mind, I thought I would start
12 with the personal income tax side of the proposal, and
13 then Chris would move into the discussion of the business
14 net-receipts tax.

15 Chris, do you want to add anything to start off
16 with?

17 COMMISSIONER EDLEY: Thanks, John.

18 I certainly subscribe to exactly every word
19 that John just spoke.

20 We have put a considerable amount of time into
21 this. In my case, I had a lot of furlough days that I
22 could use for the purpose, even though some of that time
23 was taken up helping draft President Obama's speech last
24 night, especially the parts about bipartisanship.

25 At this stage of my life, I try to avoid being

1 involved in quixotic ventures, and this surely looked
2 like that back in October or November when Speaker Bass
3 called me to talk to me about it. And I only agreed to
4 serve because it was the first thing she asked me to do,
5 and I couldn't say no, and because of my confidence in
6 Gerry Parsky's leadership.

7 But I do think it is absolutely the case that
8 almost as important as putting forward a sound package
9 of proposals, in my mind, is the importance of trying to
10 model good behavior for what strikes me as a rather
11 dysfunctional state of governance in Sacramento.

12 The spirit of bipartisan struggle that has
13 characterized most of our discussions, I think, is in
14 that vein. And I certainly hope that it can hold until
15 we cross the finish line. But it doesn't mean that
16 everybody's going to be comfortable with what we produce.

17 The only way to have a package that people could
18 feel reasonably comfortable with is if it did basically
19 nothing. That any effort to try to be bold, particularly
20 bold in the policy directions that I think the State needs
21 for the coming decades, is going to be fraught with
22 uncertainty, and that produces anxiety. And it's also
23 going to require that people compromise their initial
24 strongly felt policy preconceptions. I don't want to
25 disparage them by calling them ideological commitments,

1 but strong policy preconceptions.

2 I don't think any of us would have been asked
3 to join this commission but for the fact that we have
4 strong views about public policy that we've held through
5 our professional lives. So part of our challenge is to
6 be willing to engage each other, recognizing that there
7 are those strong commitments, recognizing that there is
8 a lot of uncertainty, but also recognizing that the only
9 way to move forward is to, in good faith, compromise
10 where compromise is necessary and possible, provided we
11 can have a basic level of confidence in our direction.
12 I think that's the nature of politics, that's the nature
13 of complex public policy-making.

14 John?

15 COMMISSIONER COGAN: Thank you, Chris.

16 So let me begin with our little walk-through of
17 the package. And then if, when we get done, if you have
18 questions, we can get Mark and Phil up here and join in
19 with us to try to answer any questions you might have.

20 I have a little slide deck here that Chris and
21 I will work off. If you'd go to page 2, that summarizes
22 the package. And we do see this as a package. Very
23 important, all the parts fit together. And it would be
24 inappropriate to consider one part in isolation from the
25 others.

1 And so the package really has four key tax
2 components and one rainy-day fund, which is not really a
3 tax component.

4 So if you go to the next slide.

5 Thanks, Michelle.

6 MS. QUINN: Is that it?

7 COMMISSIONER COGAN: That's it. Thanks.

8 So the four key tax provisions are rather
9 sizable and dramatic reduction in personal income taxes
10 across the board.

11 The second element is elimination of the
12 current corporate income tax code for businesses.

13 Third, elimination of the state sales tax.

14 And fourth, to achieve a revenue-neutral
15 package, we would replace the corporate tax and the
16 retail sales tax with a new "business net-receipts tax."

17 So if you go two more slides.

18 This slide shows, after all is said and done,
19 how the distribution of revenues changes for the state.
20 And there's only one really important point to make from
21 this chart, in my mind, and that is that the reliance of
22 the State on the personal income tax, which is the most
23 volatile part of our revenue system, declines by about
24 30 percent. And so the bulk of what we achieve in
25 reductions in volatility comes from reducing the reliance

1 by the State on the personal income tax and then, to some
2 extent, on the corporate income tax, but primarily, on
3 the personal income tax side.

4 How much volatility reduction do we get? The
5 next chart shows how much we get.

6 What this shows is the variance in State
7 revenues, estimated what they would be under the proposed
8 plan, or the plan under consideration, compared to what
9 they actually have been over the period -- I think it's
10 1996 to 2007. And what this shows, is that we would
11 achieve a 42 percent reduction in the variance in income
12 tax revenues or state tax revenues over this ten-year
13 period. And so the reduction in volatility is quite
14 extraordinary.

15 So if we go to the next slide -- yes?

16 COMMISSIONER DE LA ROSA: Can I ask a question?

17 CHAIR PARSKY: Yes.

18 COMMISSIONER DE LA ROSA: Is that the volatility
19 of the PIT only or of all state tax revenues?

20 COMMISSIONER COGAN: All state tax revenues.

21 COMMISSIONER DE LA ROSA: Thank you.

22 COMMISSIONER COGAN: All right.

23 COMMISSIONER BOSKIN: Measured at the
24 coefficient of variation, which is the standard deviation
25 divided by the median.

1 COMMISSIONER COGAN: Thank you, Michael.

2 COMMISSIONER DE LA ROSA: I knew that.

3 CHAIR PARSKY: From one economist, that
4 clarifies it.

5 COMMISSIONER COGAN: Okay, so if we go to the
6 next, the next slide describes what we have in mind for
7 the personal income tax. We would replace the current
8 complex code with a two-rate system, really a three-rate
9 system.

10 But the first rate would be 2.75 percent for
11 taxable income, up to \$28,000 for single individuals and
12 \$56,000 for joint filers.

13 CHAIR PARSKY: Michelle, could you just go back
14 one more page?

15 COMMISSIONER COGAN: One more, Michelle.

16 CHAIR PARSKY: I think you have to go back
17 one page.

18 COMMISSIONER COGAN: One more.

19 CHAIR PARSKY: There you are. Stay right there.

20 COMMISSIONER COGAN: Okay, got it?

21 CHAIR PARSKY: Yes.

22 COMMISSIONER COGAN: In any event, then we
23 would replace all of the current tax deductions and tax
24 credits that are in the California personal income tax
25 code, with a more simple approach. For single

1 individuals, we'd have a standard deduction of \$22,500;
2 and for joint filers, a standard deduction of \$45,000.

3 So a way to think about this is that, for a
4 joint filer, your first \$45,000 dollars of income is
5 nontaxable. Then the next \$56,000 of income, bringing
6 you up to over \$100,000 of income, would be subject to a
7 2.75 percent tax rate.

8 For joint filers above that \$100,000 or
9 \$101,000 threshold, you would pay a 6.5 percent rate of
10 taxation.

11 We would retain the constitutional 1 percentage
12 point addition to the personal income tax code. So the
13 so-called "millionaire's tax" would be retained in the
14 code. So for those with incomes in excess of a million,
15 they would be subject to that tax.

16 As I said, we would sweep away the current
17 credits and deductions that are in the code, except for
18 three: Mortgage interest, property taxes, and charitable
19 contributions. In addition, above the line, employee
20 benefits, would continue to be excluded from the tax
21 system as they are now.

22 But at the end of the day, you'd have
23 essentially a three-rate system with very few deductions
24 and no credits. And our hope here is to achieve a very,
25 very simplified tax code, one where you could really fill

1 out your taxes on a single piece of paper, if not a
2 postcard.

3 As you know, many on this commission had the
4 idea initially of a flat tax. We moved away from the
5 flat tax, as Chris said, in the interest of achieving
6 some compromise among the various groups. We heard some
7 very strong feelings from people about maintaining
8 progressivity in the code.

9 And so let me turn to the next slide --
10 Michelle -- which summarizes the tax reductions that the
11 plan would achieve for various AGI groups. And there
12 are two messages from this.

13 If you look at the column labeled, "Percentage
14 Reduction," you will see that each and every AGI group
15 receives a reduction in their income tax liability. And
16 if you look at the groups from \$75,000 and above, it's
17 pretty much a constant reduction of around 29 to
18 30 percent across those groups. So these reductions are
19 substantial, they're broad-based, and they apply to each
20 and every income group.

21 Essentially, this tax change on the personal
22 side that we've proposed preserves the existing degree
23 of progressivity in the code. That is, we have
24 constructed a package that reduces volatility in the
25 code by lessening the State's reliance on the personal

1 income tax as a source of revenue rather than reducing
2 the proportion of personal income taxes that are paid by
3 the highest income groups.

4 And so the goal here in constructing this
5 package -- and I think it's a goal that Chris shares --
6 was to try to get a package that would be acceptable to
7 all of you. And we ended up with one that retains the
8 degree of progressivity in the current code.

9 And I would say this: There are many people
10 that point to the fact that if you look at people over
11 \$200,000 of income, they pay 50 percent of all of the
12 personal income taxes at the current code. Under our
13 revised proposal, those individuals will amount to about
14 3 percent of all taxpayers would continue to have the
15 burden of about 50 percent of the personal income taxes
16 paid in California.

17 And so with that, let me stop and turn it over
18 to Chris for any comments he wants to make on the personal
19 income tax side, and then to describe a little bit the
20 new business net-receipts tax.

21 Chris?

22 COMMISSIONER EDLEY: Let me make two or three
23 points.

24 One is that while I have never been a subscriber
25 to the flat tax as a matter of policy, I do, as a general

1 matter, think that lower marginal rates are better
2 economic policy. Fewer distortions, better incentives
3 for growth. So I think the reduction in the marginal
4 rates is something to be celebrated. That's point
5 number one.

6 Point number two is, while I'm fully satisfied
7 with the distributional impact of these changes in the
8 PIT, there remains the question of the distributional
9 impact of the package as a whole. And I hope, Gerry,
10 we'll get to talk about that a little bit more in these
11 conversations. We don't have all the data yet, to be
12 candid about it. But just on its face, my concern would
13 be that the PIT is fine; but by implementing a BNRT and
14 eliminating the corporate tax, there is a chance,
15 depending upon your theory about the incidence of these
16 various taxes, there is a chance of losing some of the
17 progressivity of the tax system as a whole. We don't
18 know for sure. And I think even when we have more data,
19 it's still going to be largely guesswork as to the
20 magnitudes involved because there is so much mystery
21 about the ultimate incidence of these various taxes.

22 Having said that, I would at least like to
23 personally reserve the possibility of coming back to the
24 package as a whole, to tweak it in various places,
25 perhaps in the PIT, to ensure that, especially from the

1 perspective of, if you will, the blue-collar segment of
2 the income distribution, our progressivity goals are
3 achieved.

4 And finally, we have not done as much as some
5 would like in terms of making it flat. We have not done
6 as much as some would like in terms of -- I think Michael
7 is going to talk later about the value of trying to bring
8 everybody into the income-tax system; and we have not --
9 we've not achieved that. But I think we've achieved a
10 lot in the package, as a whole, that I hope speaks to the
11 full spectrum of views on the Commission.

12 Let me plunge into the BNRT quickly, so that
13 we can get to the discussion, if you will. I think the
14 changes in the sales tax, sales and use tax are pretty
15 straightforward. We don't need to review that.

16 The change in the corporate tax is pretty
17 straightforward. We don't need to dwell on that because
18 we would simply eliminate it if, indeed, we can reach
19 agreement on the BNRT as a substitute revenue source.

20 So here's the notion of the BNRT, which is a
21 form of subtraction method VAT. So as we've discussed
22 repeatedly, the basic form of it is to take all gross
23 receipts from all sources, and subtract -- that is to
24 say, take a deduction for all purchases from other
25 businesses and then apply the BNRT rate.

1 Now, just not to hide the ball, we estimate --
2 the best estimate we have at this point for the package
3 as a whole to balance out and be revenue-neutral, for us
4 to achieve the reductions that John just described in the
5 PIT, eliminate the bulk of the sales tax, the corporate
6 tax, we would need a BNRT rate of approximately
7 4.2 percent. Approximately 4.2 percent.

8 Importantly, this would apply to all businesses,
9 doing business in California. In other words, it would
10 apply to businesses even if they are, under current law,
11 pass-through entities. So it would apply to partnerships,
12 LLCs, S-corps. All business entities would pay the
13 business net-receipts tax.

14 Nonresident firms would pay the business
15 net-receipts tax on their apportioned California receipts
16 and less their apportioned deductions. Nonresident firms
17 would be subject to an economic-presence test, which we
18 are reasonably confident will pass Supreme Court muster.

19 Using the unitary method, so that related
20 entities would be grouped together for BNRT purposes, an
21 important purpose of the unitary-method test is to make
22 sure that there's some sense to the filing thresholds and
23 the liability thresholds.

24 And are those on the next page? No.

25 So just to mention those.

1 What we have in mind is a liability threshold
2 of \$250,000 in net receipts and a filing threshold of
3 \$500,000 in gross receipts. So to unpack that.

4 If you're a small business with less than
5 \$500,000 in gross receipts, you don't even need to file,
6 and there's no minimum tax. End of discussion.

7 If you have more than \$500,000 in gross
8 receipts, then you have to file, and you will have tax
9 liability if your net receipts exceed \$250,000. And,
10 again, those same thresholds apply to the apportioned
11 California elements of a multistate or a multinational
12 firm.

13 For that apportionment, John and I are proposing
14 the single-factor sales apportionment that was adopted by
15 the Legislature a couple of years ago, would becoming
16 effective in, what, 2011?

17 COMMISSIONER COGAN: Right.

18 COMMISSIONER EDLEY: So, anyway, we're just
19 sticking with that policy adjustment that the Legislature
20 made so recently.

21 We are proposing that the R & D credit that is
22 a part of the current corporate tax, be included in a
23 modified form in the business net-receipts tax.

24 And let me be clear about this: While I think
25 John and I agree that we should eschew tax expenditures

1 and designated revenue streams going to particular
2 purposes, et cetera, as a commission, we viewed the R & D
3 tax credit as somewhat different for a couple of reasons.
4 Not just that it's in current code, because lots of stuff
5 are in current credit code that we're getting rid of,
6 but also because we think in the California economy, the
7 importance of start-up firms and venture capital and
8 high-tech and so forth, the R & D tax credit in
9 combination with this small business attention that we've
10 given through the \$500,000 filing threshold and the
11 \$250,000 liability threshold will be both substantively
12 and politically useful in the package as a whole.

13 Now, let me turn to the very important and
14 complicated issue of the phase-in, because I think this
15 is what we've struggled with a lot, trying to address
16 both the issues of equity from the standpoint of business
17 taxpayers, the issue of administrative burden for
18 taxpayers, and our uncertainty -- our necessary
19 uncertainty, our unavoidable uncertainty about the
20 revenues that will be produced by the BNRT in comparison
21 with current law.

22 So the phase-in that we're proposing is that a
23 phase-in over a five-year period beginning in 2012 with,
24 in Year 1, a BNRT rate of 1.6 percent, which we estimate
25 will be sufficient to eliminate the corporate income tax

1 and make a significant down payment on reductions in the
2 personal income tax rates, plus some wiggle room. And
3 then that BNRT rate would increase each year until
4 finally set in Year 5. Period, paragraph.

5 During the course of a year, we have the
6 ability to adjust the sales tax midyear, third or fourth
7 quarter, in order to -- as a safety valve, if it's
8 necessary, to true-up the revenue that's being produced
9 to meet the start of fiscal-year projections in the
10 budget.

11 Let me just kind of repeat that idea. The
12 notion is that in a given year -- let's say Year 3 --
13 if the BNRT, established by statute for that year, is
14 not producing revenue adequate to make the package
15 generate the revenue that current law would have
16 generated, predictably, then the sales tax would be
17 adjusted -- the state component of the sales tax would
18 be adjusted in the third or fourth quarter in order to
19 generate any needed revenues to make sure that the
20 package is revenue-neutral in that year, and that we're
21 not underperforming in the production of revenue.

22 And then finally, I think what we'd like -- I
23 want to confirm with Mark and Phil and John -- but I
24 believe where we left it, was that the notion that the
25 final BNRT rate in Year 5 would be established, informed

1 by the data from the first three years of tax-return data
2 from the income tax, the sales tax, and the BNRT, to make
3 sure that we are still revenue-neutral as a package; and
4 that the final BNRT rate is producing what we need in
5 order to be revenue-neutral on the downside as well as
6 the upside.

7 So what we've tried to build in here is a
8 phase-in structure that will produce the revenues as
9 promised, while giving taxpayers and the administrative
10 system the time needed in order to adjust.

11 A couple of little details:

12 Net operating loss carry-forwards, which are
13 important to many businesses, the notion is that those
14 would be used during this period and they would die.
15 That's to say, your net operating losses accumulated
16 under the corporate income tax would wither away over
17 this five years as the corporate tax itself disappears.
18 There would be carry-forwards under the BNRT. Different
19 tax, still the possibility of.

20 Now, maybe I -- should I subside there, and
21 we'll get into the details -- more details in the
22 conversation?

23 Mark or Phil, any big things about the BNRT I
24 should put out on the table at this point, or, Gerry,
25 before we get to the discussion?

1 CHAIR PARSKY: The only other thing I would add
2 there, and then I just want to cover one other element,
3 is that it is contemplated in this transition period
4 which, as Chris mentioned, wouldn't start until 2012,
5 that in the first year, the corporate income tax would
6 have been eliminated. And, therefore, the use of the
7 tax -- of any NOLs wouldn't be usable against that tax,
8 which will have been gone.

9 And so what we are contemplating or what we
10 are suggesting for review by the Legislature, is that we
11 would allow those companies that had accumulated losses
12 to continue to utilize them over a 20-year period against
13 the BNRT, with a limitation that the BNRT liability, in
14 any given year, wouldn't be reduced by more than
15 5 percent. That's a way in which we would accommodate,
16 if you will -- or suggest accommodating those businesses
17 that had accumulated NOLs.

18 COMMISSIONER EDLEY: Can I just -- and let me
19 just say a little bit about the reasoning there.

20 We heard from so many witnesses and in so many
21 letters about the importance of these NOLs on balance
22 sheets, especially in the high-tech field and for
23 start-ups, that we were loathe to kind of wipe out that,
24 at least balance-sheet value wholesale.

25 On the other hand, we are transitioning to a

1 new form of tax. And NOLs will continue to be available
2 for federal tax liability purposes. So what we're really
3 trying to do here is strike a balance in the equities.
4 That's all there is to it.

5 And, look, let me say something -- if I can
6 put my -- speaking as a Democrat, why this --

7 CHAIR PARSKY: You're a Democrat? Are you a
8 Democrat?

9 COMMISSIONER EDLEY: Believe me, yes, I am --
10 and not one of those blue-dog Democrats, either. I'm a
11 real Democrat.

12 In fact, I'm a tax-and-spend Democrat, but...

13 So here's why I like the BNRT -- and I'm
14 speaking to my Democratic colleagues here: First of all,
15 I think it's good economics to have a VAT as opposed to a
16 profits tax.

17 Secondly, I think it's good economics to have a
18 lower marginal rate than our current corporate tax does.

19 Third, I think it's great politics for Democrats
20 to vote to eliminate the corporate income tax, especially
21 if it's in the context in which the aggregate
22 progressivity of the tax structure can be maintained.

23 Fifth -- fifth? Fifth, frankly, this is the
24 only part of the package that, to me, speaks to the
25 21st century, because it's broadening the tax base to

1 include services, which we know is going to be the growing
2 part of the economy, and doing so at a low tax rate, doing
3 so in a way that is neutral with respect to the form of
4 the business, to reduce the gaming that occurs as between
5 partnerships and LLCs and S corps and C corps and so
6 forth. And I would wager that, while Europe has been
7 using a VAT forever -- the world has been using VATs
8 forever, the U.S. is not, but I believe that this is the
9 future. Certainly on the commercial, on the business
10 side, and ultimately, I hope on the individual side.
11 So for all of those reasons, as a Democrat, I think that
12 this package makes a great deal of sense.

13 CHAIR PARSKY: Just one other comment I would
14 make, or make sure that people keep in mind. The phase-in
15 approach is gradual. It's over a five-year period. And,
16 obviously, if the Commission chooses to recommend this,
17 it's a recommendation for the Legislature to go through
18 extensive hearings on a subject that is new and is
19 transforming.

20 The only other thing I would add before we turn
21 to questions, as part of this part of the package, we've
22 had discussions back and forth -- and there are very
23 different views on this Commission -- on the subject of
24 volatility, and whether or not volatility can be addressed
25 on the revenue side, i.e., of the personal income tax

1 being the most, the largest component, and the
2 capital-gains part, along with bonuses and stock options
3 as contributing the most to that side; and, on the other
4 hand, the expenditure side, in particular, the creating
5 a reserve fund.

6 Rather than continue the debate in terms of
7 one or the other, part of this package is the next element
8 on this screen, and would be included if the Commission
9 so supported as in Section 2 of the recommendations, is
10 the establishment in conjunction with this new system of
11 a rainy-day fund, because I don't think anyone believes
12 that the recommendations made will eliminate all
13 volatility.

14 You saw the chart that would show how volatility
15 could be reduced, but we still will have within the
16 personal income tax, for instance, capital gains and
17 stock options and bonuses that may fluctuate as the
18 economy fluctuates. So part of the package and part of
19 the recommendation is the establishment of a clear,
20 strong rainy-day fund as outlined, and is further outlined
21 in some detail.

22 So we would increase the target for the reserve
23 from 5 percent of revenues to 12½ percent of revenues.
24 Require the revenues above a ten-year trend to be
25 deposited into reserve. Restrict the Governor's ability

1 to suspend transfers in the reserve. Transfers into the
2 reserve could only be suspended when revenues are
3 insufficient to provide spending at the prior year's
4 level, adjusted for the changes in population and
5 inflation. Create more stringent controls for the
6 withdrawal of reserve funds. Reserve funds could only
7 be used for natural disasters and to maintain spending
8 levels -- spending at prior year's level, adjusted for
9 changes in population and inflation.

10 And this recommendation, which we would hope
11 and urge that the Legislature vote to place on the ballot
12 for a constitutional change, would be part of the package
13 that we would request.

14 And so in combination with the changes made in
15 the personal income tax, I think the recommendation would
16 go a long way, if you will, if not get to almost parity,
17 with removing volatility from our system, and allow the
18 policymakers to, with a high level of precision, predict
19 the availability of funds over periods of time in the
20 general fund, out of which it's their responsibility to
21 decide how money would be spent. That's this part of the
22 package.

23 Okay, let's just pause. And let's ask
24 commissioners -- let's divide up our dialogue into kind
25 of two parts. Let's start with questions.

1 And I'll ask the representatives of the
2 Franchise Tax Board -- Mark, Phil, Mike -- to be available
3 where John, Chris, certainly I won't be able to answer
4 questions.

5 And, Becky, you'll be given permission, too,
6 as we go through this. If you would just hold on for a
7 little bit, we will see who around the table have
8 questions.

9 COMMISSIONER MORGAN: I'm still here. I have
10 two questions when it's my turn.

11 CHAIR PARSKY: We'll call on you for sure.
12 We'll start with Monica.

13 COMMISSIONER LOZANO: Thank you, Gerry.

14 And I'll save my observations and comments for
15 that section. But I do just want to recognize all the
16 hard work that's gone into this and thank those of you
17 that led us through the presentation.

18 So because the reduction in the personal income
19 tax works in tandem with the new business net-receipts
20 tax, I've got questions about how the rates were set.
21 Because -- and John, this is probably for you or our
22 speakers -- so it's 2½ and 6½ on the PIT, but the
23 materials that we've gotten as it relates to the business
24 has gone from 3 to 4½ to 4.2. And so it appears that you
25 first set the rates for the personal income tax and then

1 are modifying the business net-receipts rates to fill in.
2 But if you could just help me understand how you are
3 setting these rates, what the ultimate goal is, obviously,
4 is to maintain neutrality on the revenue side. But just
5 spend some time on rate-setting, please.

6 COMMISSIONER COGAN: Thank you, Monica.

7 I don't think there was a conscious decision
8 to start with a 6.5 percent rate and then figure out
9 residually what the BNRT rate would be.

10 The problem with the BNRT rate -- and this is
11 a concern, I think, that everybody has -- is that there's
12 an awful lot of uncertainty about what the estimate means
13 and how certain we are about the estimate that we've come
14 up with. What we have right now is a preliminary
15 estimate.

16 The preliminary estimate is, as you said, right
17 now in the range of a little bit above 4 or 4.2. But as
18 the estimators go back and review it in the context of
19 the rest of the package, if that rate rises, that would
20 be a cause for very serious concern about the BNRT.

21 The benefit of the BNRT is that it's a broad
22 base and, more importantly, a low rate.

23 The concern that a lot of commissioners have
24 is if that rate starts creeping up, then you have washed
25 away the major economic benefit of the package.

1 And so as far as I'm concerned, if as the staff
2 finalizes that rate estimate, if that rate were to begin
3 to creep up significantly, I think we'd have to go back
4 and look at other parts of the package, which might
5 include the income tax rates. But where we stand right
6 now -- and I know an awful lot of work has gone into it --
7 is to try to get a reasonably solid estimate of the BNRT
8 rate. And it's somewhere in the neighborhood now, we
9 think, of 4.2. Maybe a little bit less, maybe a little
10 bit more. But you can see the uncertainty. It's not
11 nailed down.

12 COMMISSIONER LOZANO: So, and I worry about the
13 adjusting along the way. Because one thing I heard you
14 say is that, in fact, we would use the sales tax to fill
15 in any resulting lower revenues being collected.

16 And so as this thing plays out -- and I
17 understand there's a transition period -- I'm particularly
18 concerned about not having set a rate, or at least a
19 consensus within the group that should it go beyond a
20 certain point, we'd bring the entire package. Because it
21 all has to work in tandem, I'm very concerned about it.

22 CHAIR PARSKY: One thing I would say about the
23 process that was undertaken with respect to the personal
24 income tax, we started with the goal -- with several
25 goals: Simplification and reducing the overall dependence

1 that the general fund has on the PIT, and then added to
2 it everyone getting a reduction.

3 And so the variables in that equation relate
4 to: Are you going to retain deductions and credits and
5 not simplify things? How are you going to set the
6 standard deduction? And how are you going to set the
7 rates, the three rates?

8 And so they are variables. And each time you've
9 got a run, if you will, on what impact you had to assess
10 were we accomplishing all of those goals. And this is
11 where we settled on a proposal that would accomplish all
12 of those goals. And we went through a myriad of different
13 iterations, many of which got increases for some levels
14 and left. So it wasn't -- I mean, it was all around those
15 objectives.

16 The BNRT rate, if you will, drives a lot of
17 concern for those of us that have looked at it because of
18 the uncertainty of predicting a new form. That's why this
19 transition is so important, that's why we have been
20 thinking about how we could potentially embody an entity
21 to reevaluate the interplay between the sales and the
22 BNRT. But you've identified -- but that's how the
23 personal income tax rates were determined.

24 COMMISSIONER EDLEY: So I want to tell a
25 different story. Some of this has a nice Rashomon kind

1 of quality to it. So here's what I thought I was
2 experiencing. What I thought I was experiencing was that
3 a bunch of whackos to the right, like Parsky, said they
4 wanted as flat a tax as possible, as simple a tax as
5 possible, with marginal rates as low as possible.

6 CHAIR PARSKY: You people up there, don't use
7 the word "whacko," unless you put a smile around it from
8 the media.

9 COMMISSIONER EDLEY: W-H-A-C-K- -- no, so --
10 right.

11 And so then what I was saying is, look, you can
12 have as much of that as you want, provided you don't do
13 damage to progressivity, which was the main horse that
14 I was fighting with.

15 So Gerry very -- doing very well said, "Okay,
16 let's come up with some options, and let's see how much
17 of the simplification, and how much of the rate reduction
18 we can do, conditioned upon making sure that everybody
19 gets a tax cut, and overall progressivity is sort of in
20 the ballpark."

21 And so I really see it as -- I really see where
22 we came out as the product of these balancing of values
23 to --

24 CHAIR PARSKY: And I will now let Michael Boskin
25 talk about how I damaged him in this process.

1 But go right ahead.

2 COMMISSIONER BOSKIN: I'm going to save that
3 for the second set of generics. I'm going to honor your
4 request and stick to specific questions.

5 But I think I can help answer why the sales tax
6 is the wiggle factor. It's the only tax that's easily
7 adjusted late in the tax year.

8 CHAIR PARSKY: That's right.

9 COMMISSIONER BOSKIN: So, for example, in the
10 third quarter and the BNRT is raised, it looks like it's
11 going to be a little bit short, you can have the sales
12 tax come down a quarter percent rather than a half cent,
13 right, without having it go up and, therefore, be a tax
14 increase and get into all that sort of stuff.

15 COMMISSIONER EDLEY: As opposed to the lag that
16 the income tax filing --

17 COMMISSIONER BOSKIN: So, now, there's still
18 the issue at the end of five years of this BNRT rate. So
19 that's a clarification.

20 But picking up on what Monica said, you know,
21 we are met at a time of revenue collapse and great fiscal
22 stress, and we are charged with dealing with kind of a
23 long-run tax structure. And I think, inevitably, we've
24 been heavily influenced by the climate in which the State
25 has found itself in recent times, sadly, for various

1 reasons. We might not agree on all the reasons, but some
2 of them are pretty self-evident.

3 But it seems to me one of the things that's
4 important as we look out to something that's going to
5 start in 2012 -- which hopefully will be pretty close to
6 normal economic times rather than late in a recession or
7 early in a recovery or something of that sort; and the
8 years, a five-year phase-in and going forward and all that
9 sort of stuff -- is to contemplate that things might be
10 very different than you're thinking about now.

11 So my first question is, what happens if the
12 BNRT or any of these other things produce more revenue
13 than was projected? All the attention has been on what
14 happens if it's less.

15 COMMISSIONER COGAN: So the idea might --

16 COMMISSIONER BOSKIN: But it's only if it's
17 above a ten-year trend line, and so it's unclear if the
18 projection is equal to the ten-year trend line.

19 So if the projection is below the ten-year
20 trend line, you could produce more and it won't go into
21 the rainy-day fund. So I think we need some clarification
22 of that.

23 COMMISSIONER COGAN: So I think what we tried
24 to do is whatever that revenue-neutral amount is that we
25 project -- and I think it would be as under the current

1 system, adjusted year by year for economic conditions --
2 I think the slack variable has to be the sales tax rate.
3 And that is, if we're producing more revenue -- and I get
4 your point -- if we're producing more revenue than we
5 have estimated, then the question becomes, should the
6 priority be to reduce the sales tax or put the money into
7 the rainy-day fund.

8 Now, from my standpoint, I would have the sales
9 tax reduction during that transition period. That's just
10 one commissioner. It's a very good question.

11 COMMISSIONER BOSKIN: And there's also the
12 question at the end.

13 COMMISSIONER EDLEY: Before we get to the end --

14 COMMISSIONER BOSKIN: There's also the question
15 at the end.

16 COMMISSIONER EDLEY: Before we get to the end,
17 it seems to me that just as a matter of legislative
18 procedure, if we want a package that can be adopted by a
19 majority vote, that it's going to have to be scored as
20 revenue-neutral over the scoring window, which I think
21 means the barometer is -- so the barometer is whether or
22 not our package is producing the revenues that, at the
23 beginning of the year, one would have forecast under
24 current law. And if that turns out to be high -- I mean,
25 if what current law would have produced is above the

1 ten-year average, then, it seems to me, it would go into
2 the rainy-day fund. Because what we've said is, it's
3 going to be revenue-neutral with respect to current law.
4 If current law were going to generate a surplus, quote,
5 unquote, then our package would produce that same surplus.

6 A rainy-day provision is what tells us that you
7 don't spend it, you put it into the rainy-day fund.

8 COMMISSIONER BOSKIN: I think that's great, but
9 I really think it has to be laid out because both the
10 current law and the alternative less-volatile proposal
11 are very still quite sensitive to economic issues. So
12 we can try to sort of lay that out.

13 CHAIR PARSKY: True.

14 COMMISSIONER BOSKIN: I have another quick
15 comment.

16 CHAIR PARSKY: Proceed.

17 COMMISSIONER BOSKIN: Number one, I take it
18 from the write-up that we have settled on expensing rather
19 than depreciation?

20 CHAIR PARSKY: Yes.

21 COMMISSIONER BOSKIN: Just to make that clear.
22 Third, it would really appreciate --

23 CHAIR PARSKY: I should say "settled," that
24 it's recommended.

25 COMMISSIONER BOSKIN: Settled in our estimate,

1 as part of the recommendation.

2 CHAIR PARSKY: Right.

3 COMMISSIONER BOSKIN: Not that it's law.

4 COMMISSIONER EDLEY: And, of course, no
5 deduction for depreciation. So expensing initially and
6 then no deduction for depreciation.

7 COMMISSIONER BOSKIN: So then there's a
8 statement in here in describing fairness that we've
9 reduced the number of taxpayers. Could somebody please
10 explain that calculation to me? You're talking about
11 there will be several hundred thousand more business
12 entities that are now filing -- they're either tax
13 collectors if they pass it forward, or taxpayers, if
14 they're bearing part of it. Is that what you have in
15 mind? But we're not counting the many millions of people
16 that are being removed from the sales tax rolls supporting
17 the general fund?

18 Referring to under "fairness." Under
19 "fairness," there's a statement that there will be an
20 increase in the number of taxpayers.

21 MR. IBELE: That should apply to the personal
22 income tax.

23 COMMISSIONER BOSKIN: Okay, okay.

24 I would like to see a calculation before I vote
25 on anything of the number of Californians and the fraction

1 of Californians who are not paying -- who will not, under
2 our proposal, pay either income taxes or general fund
3 sales taxes. I asked for that before, and it seems never
4 to get produced.

5 CHAIR PARSKY: We should definitely provide
6 that.

7 I would also say that in the exchange back and
8 forth during the course of the last several months, a
9 number of commissioners had requested that we include
10 in the personal income tax recommendation that there be
11 established a minimum tax that everyone in California
12 should pay. There is a large percentage of Californians
13 under the current system and under the proposed system
14 that would not pay tax. And a number of commissioners
15 recommended that.

16 We, collectively, have not recommended that
17 for this package. And, again, it was part of a desire
18 on our part -- Chris, John, and I -- to put something
19 forward that we hoped everyone could coalesce around,
20 recognizing that purity wasn't possible for each and
21 every commissioner.

22 Okay, next, Jennifer?

23 And these are questions.

24 COMMISSIONER ITO: Right. And I just want to
25 appreciate, again, the time and effort you guys have put

1 into this. And I've been going -- approaching this with
2 an open mind. And I still have a couple questions. I
3 have two questions in particular just to put out there.
4 I mean, the perspective that I come, and my concerns and
5 my tentativeness about supporting something around which
6 there's a lot of risk and uncertainty, my concern is more
7 thinking about the revenue impacts in the ten and
8 20 years. And my concern being on the flip of Michael is
9 about the unintended consequences of shifting from a tax
10 structure shifted away from income and more towards
11 consumption and where we're going as an economy and as a
12 nation, if we're moving away from consumption and more
13 towards savings. My concerns come from more of what's
14 happening with the -- what is going to happen with the
15 underlying economy.

16 And so my one question is around, so are we
17 saying that at the end -- so I'm not as concerned with
18 the five-year transition, but my question is, are we
19 saying that at the end of five years, that's when we'll
20 set the rate for the business net-receipts tax and it
21 will be fixed from there?

22 COMMISSIONER COGAN: Well, I can tell you the
23 way I was thinking about it, is that we would set an
24 ultimate business tax rate in what we send to the
25 Governor and the Legislature, and treat that as our best

1 recommendation at this point. But not to leave it as
2 something to be determined by the Legislature and the
3 Governor.

4 And so our recommendation would be for a
5 specific -- and I would hope it to be sort of an upper
6 limit on any BNRT that we would think would be acceptable.

7 And my sense is, by the way, after five years,
8 at that point we should have the experience at that point
9 to know whether this thing is working. And if it's not
10 producing the kind of revenues -- if it's falling short
11 of the revenues that the current system would produce,
12 then I would think there would be a complete relook at
13 whether this is, in fact, the right way to go or what
14 adjustments have to be made in the code. That's my view.

15 COMMISSIONER EDLEY: I have a slightly different
16 view, perhaps. And I would really like to hear from the
17 staff on this.

18 The way I think about it is that suppose that
19 we're at the start of Year 5, and we're looking back at
20 the data from Years 1, 2, and 3, including the income in
21 PIT data and the corporate income tax data, and so forth,
22 so we have a pretty good sense now of how all these
23 things interrelate in practice as opposed to modeling --
24 at least a better sense. And let's say the BNRT is
25 underperforming. Then your choices are to build into the

1 legislation something automatic, so that you plus-up the
2 BNRT rate to hit the mark. That's Option 1.

3 Option 2 would be, you plus-up revenues with
4 the sales tax or the corporate income tax, or some form
5 of the corporate income tax, such as a surtax on federal
6 corporate income tax. You compute your corporate income
7 tax anyway, for federal purposes, just multiply by .2 or
8 something, and that would go to the State to try to get
9 the revenues in line.

10 Or Option 3, sunset the whole thing and make
11 the Legislature go back to square one.

12 Now, so sort of as between those, I thought the
13 simplest thing would be to build into this an automatic
14 mechanism so that the BNRT rate might be moved up or down
15 by some limited amount in order to level things out. But
16 I can imagine those other two options, and I'm really
17 kind of agnostic as between them. I would not fiddle with
18 the PIT. It would have to be one of the taxes, I suppose,
19 that's imposed on business entities; hence, either the
20 sales tax or something related to the federal corporate
21 tax liability.

22 And let me just say, I would link it to the
23 federal corporate income tax liability because these firms
24 are going to have to fill that out, anyway -- at least the
25 ones that are not pass-throughs would not have to fill

1 that out, anyway.

2 I mean, nothing is perfect, but I just don't
3 see how to --

4 CHAIR PARSKY: Well, one thing to think about,
5 a phase-in program that would work something along the
6 following lines:

7 In Year 1, we would make a determination on
8 the level of BNRT rate that we would anticipate would be
9 necessary to deal with the complete program in the year
10 2012. That's a year that specific data and projections
11 will have already been made by the Department of Finance.
12 That will result in a rate not yet to be finalized, but
13 around 4 percent, maybe a little bit less.

14 We'll have to see what that is. Let's just say
15 for argument's sake that the conclusion is 4 percent.
16 And we would suggest to the Legislature for further
17 effort, that getting to that rate, from our standpoint,
18 needs to be done on a phased approach to all of these
19 taxes over five years.

20 And in Year 1, we would seek the elimination of
21 the corporate tax entirely, costing "X." Let's just say,
22 for argument's sake, that that is between \$9.5 billion
23 and \$10 billion -- we'll have to refine that -- and a
24 down payment on the reduction in the personal income tax,
25 leaving the current system in place but just giving a

1 reduction in everyone's taxes as currently set, as if we
2 didn't make any change, of about 20 percent. That would
3 cost -- and the estimate would be somewhere in the range
4 of \$3 billion or \$3.2 billion as --

5 COMMISSIONER BOSKIN: That's 20 percent of our
6 reduction, not 20 percent of their current tax liability.

7 CHAIR PARSKY: No, 20 percent of the reduction
8 we ultimately would be seeking. The \$15 billion that was
9 shown here.

10 And 1 percent of the 5 on the sales and use
11 tax. That would result in a much lower rate in that year
12 than the 4 percent that we would ultimately say is
13 targeted.

14 It might result in this 1.6 that you mentioned.
15 We have to refine that. But it would be a very low rate.

16 And in Year 2, we would have the same sort of
17 system: A down payment on the reduction in the personal
18 income tax, and the potential for another reduction of
19 1 percent in the sales and use tax. And at each point
20 in that cycle, or in that year, we have this flexibility
21 on the adjustments in sales and use tax to see.

22 Year 3, we would put in place the, quote, new
23 system on the personal income tax, and we would have
24 another potential 1 percent reduction in the sales and
25 use tax, with some element of flexibility. That would

1 have left us with 2 percent left for Years 4 and 5 in the
2 sales and use tax to be reduced, and an incremental amount
3 of rate to be put in place for the business net-receipts
4 tax.

5 We could at that point recommend that a
6 disinterested tax group make an evaluation of the revenues
7 that have come in and not, and make a recommendation with
8 respect to how to get to the ultimate rate on the BNRT
9 and the sales and use tax which are left to be adjusted.

10 Now, Michael's point isn't quite dealt with,
11 either in Years 4 or 5, which is what happens if the
12 revenues of the BNRT are so much greater than anticipated,
13 and it doesn't get picked up, if you will, in the
14 definition of the "*rainy-day fund*." Some of your
15 colleagues may like that a lot, but it's not dealt with
16 precisely.

17 But I do think we need to suggest -- the
18 Legislature is going to refine this, without any question.
19 But I think we should suggest the sensitivity we have on
20 the lack of precision on predictability of how the rate
21 on the BNRT would work in producing revenue. And I know
22 there will be concerns from the business community, from
23 other commissioners, that suggesting that the rate on the
24 BNRT would get above a certain level, that will cause
25 concern.

1 And the Legislature, in their infinite wisdom,
2 they obviously can do what they wish. But from this
3 Commission's standpoint, I think we should be sensitive
4 on that subject.

5 On the other hand, we also want to be sensitive
6 on the fact that we need to produce a revenue-neutral
7 set of recommendations. So I think we need to think
8 about that.

9 COMMISSIONER BOSKIN: I couldn't agree more.

10 I think Jennifer and Monica made very important
11 and useful points. I would add that even if we did not
12 have a BNRT -- this is made much worse, or much more --
13 "worse" is a bad word -- it's much more salient because
14 this is a new tax and there's more uncertainty.

15 CHAIR PARSKY: Yes.

16 COMMISSIONER BOSKIN: But even if we just had,
17 as an alternate proposal, extend the sales tax to
18 services and reduce the corporate rate and the income tax
19 rates down to something like other states, rather than
20 being outlier, go to the median. That would be a much
21 less radical proposal, would help reduce volatility, do
22 some of these other things. We'd still have the same
23 thing because we're not sure what would happen out there.

24 COMMISSIONER EDLEY: Right.

25 COMMISSIONER BOSKIN: So the Legislature would

1 still have to true something up and raise or lower or do
2 it, whatever the pressures would be.

3 COMMISSIONER EDLEY: Can I try, Gerry?

4 It seems -- I think there are three buckets of
5 issues here.

6 One question is, what do you do about
7 underperformance or overperformance of the BNRT relative
8 to current law; right? So that's the revenue-neutrality
9 issue.

10 The second question is, what do you do about
11 underperformance or overperformance of the package
12 relative to the ten-year average? That's the rainy-day
13 fund issue.

14 COMMISSIONER BOSKIN: Right.

15 COMMISSIONER EDLEY: The third question is,
16 if you've got a problem with respect to Category 1, the
17 revenue-neutrality criteria, how do you do the true-up
18 or the true-down in order to get back to revenue
19 neutrality? And that's how, as in using which tax rate,
20 on which tax, and how in terms of institutionally who has
21 the authority to do it. So that's kind of 1, 2, 3A, 3B,
22 in my mind.

23 And what I was suggesting in response to
24 Michael's earlier point, is that if current law out in
25 Year 4 would have produced a boon in revenue because

1 we've had the Obama surge --

2 CHAIR PARSKY: Be careful.

3 COMMISSIONER EDLEY: Okay, Year 2, the Obama
4 surge, okay. All right, so --

5 CHAIR PARSKY: Put that in the "wacky" category
6 up there.

7 COMMISSIONER EDLEY: Okay, so in Year 3, we
8 have a surge in revenue under current law but not under,
9 with our package, then I think you have to true-up the
10 rates in our package somehow in order to mirror current
11 law, and then put the excess above the ten-year average
12 into the rainy-day fund.

13 COMMISSIONER BOSKIN: But this is all designed,
14 however, to be kind of neutral over the business cycle.

15 COMMISSIONER EDLEY: That's right.

16 COMMISSIONER BOSKIN: So I don't think you can
17 say, there's a boom. God, we really have buyer's remorse
18 now. We have a more stable tax structure, so there's not
19 a huge amount of revenue flowing in from capital gains
20 and stock options, so we have to raise other tax rates.

21 COMMISSIONER EDLEY: Well, no.

22 COMMISSIONER BOSKIN: Suppose there's a
23 double-dip. We won't blame it on Obama. Just suppose it
24 happens, okay? Then what are you going to do? The
25 revenues collapse further, but they're going to be more

1 under our proposal than they would have been. Are you
2 going to then start cutting our proposal? I think it's
3 totally symmetric. I think you can't get into that.

4 COMMISSIONER EDLEY: Well, but what do we do
5 about the requirement of revenue neutrality over the
6 scoring window?

7 *(Commissioner Pringle entered the hearing room.)*

8 CHAIR PARSKY: I just would separate in your
9 mind the need for revenue neutrality that the Legislature
10 may decide to do for purposes of voting from -- let's
11 just say that the -- because that's a projection. They
12 have to determine, based on the proposal, whether over
13 a one-year period or a three-year period or a five-year
14 period, whatever they determine they believe is
15 revenue-neutral, then they can decide how they want to
16 vote. Separate that from actual performance that occurs
17 once the law is enacted. And that is an issue that I
18 think a recommendation needs to take into account
19 adjustments if we were wrong, not because of revenue
20 neutrality, but we were wrong on the amount of revenue
21 that was to be generated. And you can have a variable
22 in the transition period to get there. If at the end of
23 five years, fully phased in, there was nothing wrong, but
24 in the next five years something happened, the Legislature
25 would have to act as they are forced to do now.

1 So I just would separate out the issue of
2 revenue neutrality as determined from the beginning from
3 some pause at the end of three years or some pause where,
4 because of the uncertainty of this tax, somebody would
5 need to determine the balance of the implementation of
6 the phase-in program, in order to try to achieve the
7 level of revenue that you anticipated.

8 COMMISSIONER EDLEY: This is really hard. It
9 may be time for a break.

10 CHAIR PARSKY: Okay, well, let's just finish
11 some questions.

12 And then, Jennifer, did you have --

13 COMMISSIONER ITO: No.

14 CHAIR PARSKY: Edward?

15 COMMISSIONER DE LA ROSA: Thank you, Chairman.
16 And thank you also Commissioners Cogan and Edley for all
17 the work that you did, for this package. It's a great
18 structure. And I'm not sure exactly how we're going to
19 arrive at a consensus, and I'm sure that many parts of the
20 package are going to be discussed today, and I'm counting
21 on Monday as well. But I had a question about one
22 particular part of it -- well, let me back up.

23 I'm very happy to see that the concepts like
24 rainy-day fund made it into this package, given the fact
25 that we had to interpret really what the Governor's

1 directions were and things of that nature. And I'm very
2 happy to see that there's been an effort, I guess, to
3 broaden the tax and lower the rate. I think that's a
4 great development.

5 And, Chris, really, this whole effort, the
6 comment that you made about making a big part of the
7 structure relevant to the 21st century economy is, I
8 think, very important as well. And I was worrying about
9 that earlier today as we walked in here.

10 But I want to go back to this personal income
11 tax change by AGI class, and I think that there was one
12 question. And I'm sure when you all were meeting, you
13 discussed this many times over. But I feel compelled to
14 answer that. And by my count, there's about 7 million
15 returns if you go up to \$75,000 of income, which is about
16 half of the number of returns in California. And those
17 returns are not participating as fully as people in the
18 other categories are in the reduction in the tax burden
19 when you measure the personal income tax.

20 When you consider that these people will also
21 be subject to sales taxes, I guess, and other taxes as
22 well, I'm concerned about really what the total tax
23 burden would be on them relative to the rest of the group
24 once a plan like this is put into effect.

25 And I believe that Jean Ross, when she made a

1 presentation one day, gave us a table that demonstrated
2 what the total tax burden is by quintile, I believe, for
3 people. And I know that there was some questions about
4 the methodology. And, of course, if there's somebody that
5 has a better way of measuring, I'd be more than happy to
6 see that slide as well. But it seems to me that it would
7 take just a small reduction in the tax break that is
8 given to the group making from \$200,000 through infinity,
9 to cover an effort to give an equal break to the people
10 making up to \$75,000.

11 And I just wondered if that's an important thing
12 for this group to consider before we arrive at the final
13 plan or not, but it was something that jumped out at me
14 when I took a look at this.

15 CHAIR PARSKY: Well, I do think John -- just to
16 remind you of John's point, and that is that the standard
17 deduction needs to be taken into account first. So what
18 we're really talking about are individuals' or families'
19 joint returns that are at \$105,000 that ticks into the
20 tax.

21 We've tried a lot of different models and to
22 try to make sure that everyone gets a reduction. And
23 it is clear that the progressive nature of the personal
24 income tax is not altered dramatically.

25 If you look at the top two categories of tax

1 returns, \$200,000 through infinity, you have about --
2 I don't know about infinity, we'll leave that to Michael
3 Boskin to decide -- but about 500,000 returns constitute
4 that group. And that group is paying the vast bulk of
5 the taxes before and after. Before and after.

6 So on the issue of progressivity relating to
7 the PIT, this was an important effort as we've gone
8 through this. A number -- several commissioners wanted
9 us not only to demonstrate that the PIT was constituting
10 a smaller percentage of the overall general fund, but
11 that the progressivity of the PIT was substantially
12 reduced. And that's not accomplished -- the second half
13 is not accomplished here.

14 Becky, did you have a question?

15 COMMISSIONER MORGAN: Thank you. I want to
16 thank Maria and all for letting me come in by phone.

17 I guess so I understand, this would take place
18 in 2012, which means five years is 2017, eight years from
19 now. That's two terms of a new governor and probably
20 80 percent of all legislators that will be voting on this
21 hopefully will be gone because of term limits. So I
22 guess I would suggest that this is a very good outline,
23 but it's probably going to change. But all the work
24 that's been done I think sets a great foundation.

25 Now, just a couple questions on the PIT. As I

1 understand, there will be no carryover for charitable
2 deductions. You take what you give in one year; and then
3 if you give more, you can't carry it over? Or is there no
4 limit on what you can deduct?

5 CHAIR PARSKY: I'm not quite sure I understand
6 that.

7 COMMISSIONER EDLEY: If deductions exceed gross
8 revenues.

9 CHAIR PARSKY: Oh, right.

10 COMMISSIONER EDLEY: If deductions exceed gross
11 revenues, you would have a carryover --

12 COMMISSIONER COGAN: The PIT.

13 COMMISSIONER EDLEY: Oh, I'm sorry, are we
14 talking about the PIT?

15 COMMISSIONER POMP: We should all have that
16 problem, by the way.

17 COMMISSIONER MORGAN: I'm sorry. I can't hear.

18 CHAIR PARSKY: Carl, do you have an answer to
19 that question?

20 MR. KUSIAK: I'm Pat Kusiak with the Franchise
21 Tax Board.

22 The language drafted, that was drafted related
23 to charitable deductions, essentially creates charitable
24 deductions under the new approach, just as they are
25 treated under the old law. There's no change.

1 COMMISSIONER MORGAN: Okay, so there is no
2 limit on what you can deduct for charitable contributions,
3 assuming you give it away?

4 MR. KUSIAK: To the extent there is no limit
5 under current law, there would be no limit under the new
6 law. There are some limits under current law, but
7 they're very narrow in scope.

8 COMMISSIONER MORGAN: Okay, because there are
9 limits federally.

10 And then on the chart that has all the numbers
11 of taxpayers and the percentages and the reduction in tax,
12 those numbers are from 2007 or are they in 2014?

13 COMMISSIONER BOSKIN: They're from 2014.

14 COMMISSIONER MORGAN: So these are the estimates
15 for five years from now?

16 COMMISSIONER BOSKIN: Yes.

17 COMMISSIONER MORGAN: Okay. And on the
18 business, did I hear correctly, because it was one of my
19 questions, that there is no deduction for depreciation?

20 COMMISSIONER BOSKIN: To expense the first-year
21 expenses.

22 CHAIR PARSKY: Well, you have, in the current
23 year of purchase, full expensing.

24 COMMISSIONER MORGAN: Okay, full expensing.

25 COMMISSIONER BOSKIN: Because there's nothing

1 left to depreciate.

2 COMMISSIONER MORGAN: Okay. Then I would just
3 want to go on record, in case there's not time to get
4 back, with Michael Boskin and anybody else that would
5 come on board, that I think every person in California,
6 that is working in California, should have a stake in
7 our state. And that stake is best represented by having
8 a minimum tax, whether it be \$50 or 1 percent of AGI or
9 something.

10 And it's been my experience as an elected
11 official, that when you're charged \$5 at a health clinic,
12 you take care of your health better, or a minimum charge
13 at a museum where people show up. I just really would
14 ask for a consideration of a minimal contribution in
15 appreciation of what the State provides.

16 CHAIR PARSKY: Okay, thank you.

17 Yes, John?

18 COMMISSIONER COGAN: Say, Ed, you know, you
19 raised a good point, you know, about the distributional
20 effects, because they are lower, the tax reduction
21 proportionately is lower for the lowest groups. But I'd
22 guess I'd ask you to look at it just a little bit
23 differently, if I could.

24 If you look at the \$20,000 to \$50,000 group,
25 the tax burden that they now have -- income tax burden --

1 is \$196. So that's \$4 a week.

2 If we wanted to get their proportionate
3 reduction down by 25 percent, then we reduce it by a
4 dollar. And so we reduce it from \$4 a week to \$3 a
5 week. And so to make a distributional table look good,
6 the question is, how important is it to have a \$1-a-week
7 reduction in some group's income tax? And I'm just
8 hoping that you look at it a little bit like that as
9 opposed to just be thinking that everybody has got to get
10 an equal, proportionate reduction. Just a different
11 perspective.

12 CHAIR PARSKY: Monica?

13 COMMISSIONER LOZANO: Thank you. I just have
14 one more question --

15 COMMISSIONER MORGAN: Take it down under \$2 a
16 week or \$1 a week.

17 CHAIR PARSKY: Wait, Becky, you've got to --
18 wait and let me call on you because you're not around
19 the room. So I will call on you if you have further
20 questions.

21 COMMISSIONER MORGAN: Okay.

22 CHAIR PARSKY: Go ahead, Monica.

23 COMMISSIONER LOZANO: I just have a question
24 on an issue that's not referenced in the materials, but
25 it does refer to insurance companies. And we had had a

1 conversation earlier about financial institutions, and
2 they are now, I understand, covered under this. And I'd
3 like to have some clarification about those entities as
4 they relate to the business tax now.

5 CHAIR PARSKY: Oh, I'm sorry. The financial
6 companies is an area of continuous concern. We struggled.
7 And anyone looking at implementation of the business
8 net-receipts tax I think will struggle with how to deal
9 with pure financial companies.

10 And so what we are suggesting is that they --
11 the suggestion would be that they be included under a
12 different -- a type of calculation that addresses --
13 and I'll let Carl talk about it in a little bit more
14 detail -- but addresses the net interest income for these
15 entities.

16 Although I am sure that we could have a lengthy
17 discussion among economists, in particular, as to whether
18 or not the value-added tax concept really does apply in
19 any way to financials.

20 So we are suggesting that they would be
21 included, but with a notation that further study of this
22 needs to be undertaken by the Legislature to determine
23 whether or not they should be included -- and I think
24 there is a note in -- I'm not sure, Mark, page 2, page 3?

25 COMMISSIONER LOZANO: There's a footnote, but

1 it doesn't refer.

2 CHAIR PARSKY: At least I remember reading
3 Mark's note that indicated something along those lines.

4 COMMISSIONER EDLEY: It is just to leave current
5 law. Leave current law.

6 CHAIR PARSKY: Right. One alternative is to
7 leave them subject to current law. The argument the
8 other way is that we are eliminating the corporate tax
9 entirely, to leave it in place for one body. Michigan
10 took a little different approach there.

11 But, Carl, did you have any other comments
12 about that subject?

13 MR. JOSEPH: Sure. The first comment I'd make
14 is in regard to insurance companies. Insurance companies
15 are not part of the BNRT. They pay the gross premiums
16 tax in California. They're exempted under the
17 Constitution from paying other taxes. So they're in
18 their own little world already.

19 As for the financials, what the Commission has
20 struggled with is the concept of having all taxpayers
21 within one system versus having a second special, or a
22 bold system, whichever way you want to go, for financial
23 companies. And there are a lot of issues related to
24 having them on a separate system or having them taxed
25 under the old system. Because one of the concepts that

1 is part of the BNRT is the unitary method. And in a
2 unitary method, it is quite normal for there to be
3 financials and general corporations in the same group.
4 And so when you have two groups that are having their
5 either income or net receipts calculated as a group
6 because they are functioning as a unitary enterprise, it
7 gets a little bit tricky as to how to tease them apart to
8 pay two different taxes, such that you can end up with a
9 system that's not prone to gaming, not prone to having
10 big swings, based upon one being measured by income, one
11 being measured by receipts.

12 So at this point, what the Commission received
13 some input on from various economists, was that it was
14 possible to put the financials into the BNRT if you gave
15 them, as an item of receipts, interest income and as an
16 item of deduction, interest paid. Because that is in
17 relation to their services that they are providing as a
18 financial.

19 So as it's written now, there are -- there's a
20 special definition for what is a "financial." And if you
21 fall into that category of being a financial, then you
22 have an additional item of interest receipts, but you also
23 have an additional deduction that other corporations don't
24 get. That's how it's put forth at this point. But,
25 obviously, you heard from Chair Parsky, there are other

1 ways to look at this.

2 CHAIR PARSKY: Fred?

3 COMMISSIONER KEELEY: Thank you, Mr. Chairman.

4 Mr. Chairman, let me start with thanking you
5 and Commissioner Edley and Commissioner Cogan for all the
6 hard work that you've put into this. I know this is
7 compound, complex, difficult; and you folks have put in
8 front of us a thoughtful package, and a package that
9 I'm glad we are going to debate and discuss it. And also
10 thanks to the staff for their fine work which went on day
11 and night, I'm sure, to get this in front of us today.

12 Mr. Chairman, let me ask a couple questions
13 about how the personal income tax recommendation that
14 you're making would treat a couple of issues. Under
15 current law in California, Social Security income is
16 exempt.

17 Is it your thought that Social Security income
18 would be exempt from personal income tax under the new
19 architecture that you're proposing?

20 CHAIR PARSKY: Yes.

21 COMMISSIONER COGAN: Yes.

22 COMMISSIONER KEELEY: Good. Thank you.

23 Let me ask also, do you believe, Mr. Chairman,
24 it would be possible to have, for the Commission, on
25 Monday or before Monday, a couple of things? One is an

1 analysis by income by decile of the tax burden currently
2 and the tax burden of this package as proposed? Would
3 that be possible for us to see that?

4 COMMISSIONER COGAN: Are you talking about the
5 PIT or are you talking about total?

6 COMMISSIONER KEELEY: Total package. Is it
7 possible?

8 COMMISSIONER COGAN: *(Nodding head.)*

9 COMMISSIONER KEELEY: So Mr. Cogan is
10 saying "yes."

11 CHAIR PARSKY: I will tell you that in terms of
12 how demanding that is and how much certainty can surround
13 that, it needs to be caveated extensively.

14 COMMISSIONER COGAN: You know my views. You
15 know my view on how reliable any such estimates from the
16 BNRT are with respect to distribution. I think I've made
17 it before. I would discount them very, very heavily.

18 And for those that are concerned about the
19 distributional consequences, I would put 80 percent of
20 my weight on that personal income tax calculation, and
21 then factor in, perhaps, some retail sales tax. But I
22 don't think we have enough at all in the way of hard
23 information to give you a reliable estimate of the full
24 distributional consequences. But it can be done.

25 COMMISSIONER KEELEY: I think that's fair,

1 John, that we understand the high degree of variability
2 or accuracy or whatever it might be. But I do think it's
3 a fair question to ask for that.

4 And I'll look at every footnote that qualifies
5 it. I think that's fair enough. But I do think it's
6 also fair to ask how that would look.

7 COMMISSIONER COGAN: The numbers will appear
8 very fuzzy.

9 COMMISSIONER KEELEY: Thank you.

10 A couple of other questions.

11 When you were wrestling with the architecture
12 of the BNRT, I know that, simultaneously -- and we'll
13 hear later -- that some of us were wrestling with how
14 to put together a pollution tax. And I know in that
15 conversation, the issue arose as to what the effect on
16 transportation -- what effect there would be on
17 transportation, specifically Article 42 -- or excuse
18 me, Proposition 42, as it relates to the sales tax on
19 gasoline in California. And if there's a reduction or an
20 elimination of the sales tax, how that Prop. 42 funding
21 source, which is relied upon heavily in California for
22 transportation, what your thoughts would be about either
23 replacing that or offsetting those Prop. 42 funds in
24 some way, which are directly tied to the sales tax on
25 gasoline?

1 CHAIR PARSKY: You raise an important issue.

2 Our thoughts were that, apart from the potential
3 decision to proceed with a pollution tax, that dealing
4 with how the general fund revenues would be spent was
5 not the purview of this commission. And, therefore, if
6 there was no dedicated state sales tax on gasoline, that
7 allocation of revenue would have to be independently
8 decided by the Legislature out of the general fund,
9 because there wouldn't be a sales tax at the state level
10 on gasoline.

11 If, in the discussion of a pollution tax, that
12 is the desire on the part of the Commission, and through
13 Proposition 42, those funds would automatically be
14 dedicated to transportation, that would relieve -- if
15 the rest of the package was included, that would relieve
16 that burden on the general fund, and might enable us to
17 recommend a lower rate on the business net-receipts tax.

18 COMMISSIONER PRINGLE: Could I interrupt you
19 just a second, Mr. Chairman?

20 I would like to reserve -- first off, to all
21 of you, I want to apologize for being late. We had the
22 kickoff of D23, the largest Disney Expo in the world was
23 launched this morning. So I wanted to make sure, if you
24 would like to join the 45,000 people who are in Anaheim
25 over the next three days for D23, please do so. It will

1 be exciting.

2 COMMISSIONER EDLEY: Can I move we recess?

3 COMMISSIONER PRINGLE: Yes, you're more than
4 welcome to.

5 CHAIR PARSKY: What happened to you guys in
6 the 45,000? That would have been a much better thing to
7 witness.

8 COMMISSIONER PRINGLE: So what I would also
9 like, Mr. Chairman is, I know we are going to hear after
10 our break a presentation on the pollution, carbon
11 gas/fuels tax concept. And I'm very open to hearing that,
12 because I do have some specific interests that Mr. Keeley
13 may find interesting about this exact issue. And I'd
14 like to be able to reserve this time. Because this
15 probably isn't the right time for that, but I would like
16 to be able to talk about it at that time.

17 CHAIR PARSKY: Okay.

18 COMMISSIONER KEELEY: Thank you, Mr. Chairman.
19 Mr. Chairman, a couple of other quick questions.

20 With regard to the exemptions that have been
21 proposed in the package relative to the BNRT, I am
22 interested in hearing the reasoning for exempting the
23 nonprofit entities that you did include, what the
24 reasoning is for that.

25 As I understand it, nonprofits are subject to

1 taxation currently and subject to sales taxation.

2 And I'm wondering what the reasoning was for
3 providing an exemption for nonprofits in general, and
4 specifically, health care and education?

5 CHAIR PARSKY: Why don't you begin, and then
6 I'll pick up?

7 MR. KUSIAK: The direction from at least the
8 working group that was dealing with the BNRT, essentially
9 was aware of the fact that exempts and various exempt
10 entities are generally exempt on their income tax but are
11 subject to tax on what's referred to as "unrelated
12 business tax."

13 What's been retained is the notion of an
14 unrelated business receipts. So in that context, exempt
15 entities would continue to pay tax on unrelated business
16 receipts. So essentially, the structure was established
17 to be comparable to what the current income tax rules
18 are, but to require exempts who would otherwise be paying
19 unrelated business tax on unrelated business income, will
20 now be paying business net-receipts tax on their unrelated
21 business net receipts.

22 COMMISSIONER KEELEY: Thank you. I appreciate
23 that.

24 Let me ask another question on the financials
25 again. I understand, having served on the insurance

1 committee, the way insurance companies are taxed on their
2 premiums as opposed to being covered in some other way
3 in California.

4 So they would continue because they have a
5 constitutional privilege there, they continue to enjoy
6 that privilege, unless we had some other idea about what
7 their privilege should be or not be.

8 But as we move into the financials, where
9 Graham-Leach-Bliley essentially tore down a lot of the
10 walls between financial institutions, what banks used to
11 look like and what insurance companies used to look
12 like, and this and that, I am interested in how the
13 financials -- and I know the question was asked earlier,
14 but I'm -- at least as one commissioner, I'm not clear on
15 how they are -- how, what is being proposed, would change
16 their tax obligation for financials? How would it change
17 it?

18 MR. JOSEPH: Well, when you say "How would it
19 change it," obviously, they'd go from an income-tax base
20 to a net-receipts tax base.

21 COMMISSIONER KEELEY: Right.

22 MR. JOSEPH: So from the standpoint of how they
23 would calculate their tax, they'll be calculating it on
24 a much different basis than they calculate it now.
25 Obviously, the rate's different as well.

1 One thing we did talk about a lot, which you
2 bring up here, is the world has changed a bit as to who
3 is a financial. So the definition of "financial" that is
4 contained within the new BNRT is different than the old
5 rules that we had under the corporate code, in that it
6 picks up the definition of "financial institutions" that
7 was put together by the Multistate Tax Commission.

8 One of the things that does, is it essentially
9 treats anybody owned, directly or indirectly, through a
10 bank holding company structure, which is the new way of
11 doing things, will be deemed to be a financial
12 institution. Which the old rules that we had from
13 30 years ago, case-law rules, would not allow us to do
14 that.

15 So we will have better parity between various
16 competitors in the financial industry, in that they will
17 all use the same base for net receipts, which is not
18 necessarily the case now under the income tax.

19 As to whether they'll pay more or less, I have
20 not seen any distributional data about how the actual
21 tax calculation for any sort of standardized financial
22 institution would be in relation to what they would be
23 paying under the income tax. I have not seen anything
24 like that.

25 COMMISSIONER KEELEY: Mr. Chairman, again, if

1 it's a reasonable request -- if it's not a reasonable
2 request, I understand we shouldn't do it -- but if it's a
3 reasonable request between now and Monday, when we meet
4 again, I would at least be interested in seeing what that
5 means, especially as it relates to, if we are, in fact,
6 making a significant change in the tax on banks and we
7 are now redefining and modernizing our definition to
8 include financial services so that it's consistent with
9 the national definition, I would be interested in knowing
10 what that does relative to the tax obligation when we do
11 those two things together. We eliminate the bank and
12 corp. tax, we redefine what constitutes a financial
13 service entity, and they are no longer subject to the
14 bank and corp. tax but are now going to be subject to
15 business net-receipts tax. I would be interested in
16 seeing what happens there.

17 And since Commissioner Edley -- period,
18 paragraph -- was able to wave his bonafides, as a good
19 liberal Democrat, what I'll say in my own case, is that
20 my observation, having served in the Legislature and
21 watching nationally the recent turmoil we're going through
22 financially and economically in this country, that the
23 old phrase about privatizing the profits and socializing
24 the problems seems pretty clear in the case of the bank
25 and financial services industry. That they were very

1 pleased to take all the private profits when things were
2 going well and when things didn't go well, be the first
3 ones in line to ask that we socialize their problem and
4 provide them with extraordinary amounts of bail-outs.

5 Now, whether that's good public policy or not,
6 this commission probably doesn't want to get into it.
7 I'm not necessarily opposed to the idea of having
8 recapitalized the banks. I'm not sure that that was an
9 awful thing. But I am interested, because it is within
10 the purview of this commission to see how we treat banks
11 and financial services. Because you've just indicated,
12 we're not just making one change here for them, not for
13 them, involving them; we're making three changes that
14 would involve them. And I would like to see how that
15 affects what their obligation is. So if you'd be kind
16 enough to do that, I think that would be helpful.

17 CHAIR PARSKY: Mark, what do you think about
18 the data that might be available over the next 48 hours?

19 MR. IBELE: It's a reasonable question. I'm not
20 sure what we're going to be able to do before Monday.

21 Just in terms of estimating, the Franchise Tax
22 Board, which provides the estimates on bills and statutory
23 changes and so forth, is still in the process of putting
24 their estimating model together. And that won't be ready
25 for some time.

1 What I would ask is, maybe get a clarification
2 on what's actually been requested, and then maybe we can
3 speak with our consultant during the break and see if
4 there's some way that we can come up with something
5 before Monday.

6 CHAIR PARSKY: Well, I think -- you correct me
7 if I'm wrong, Fred -- but I think what Fred is seeking
8 relates somewhat to the objective of the rate and the
9 definition that we set for the financials, namely,
10 generally speaking, to put them in somewhat the same
11 position, albeit hard to determine, that they might have
12 been under the corporate tax.

13 Now, what I think Fred is asking is, if you
14 applied the existing tax and system of definition, it
15 would produce "X." As you change the definition and
16 apply a new system and rate, does it achieve "X" or does
17 it achieve something different?

18 COMMISSIONER EDLEY: But you're looking for
19 examples, not revenue estimates; right?

20 COMMISSIONER KEELEY: Chris, what do you mean
21 by "examples"? Help me with that.

22 COMMISSIONER EDLEY: Examples. Case examples.
23 Institution A, B, C. Under current law, they'd pay this;
24 under the proposal, they'd pay that; right? As opposed
25 to saying, for the sector as a whole --

1 CHAIR PARSKY: I see your point.

2 COMMISSIONER EDLEY: -- what are the total
3 revenues that are projected; right?

4 Both, you'd like both; right?

5 COMMISSIONER KEELEY: Well, I think there's a
6 general understanding. How about I talk during the lunch
7 break, and we see if we can --

8 COMMISSIONER EDLEY: Okay, because the example
9 is going to be easier.

10 COMMISSIONER KEELEY: -- if we can agree on what
11 can be brought back to the Commission in that regard.
12 But I do think it's a worthwhile sector analysis for us
13 to look at.

14 Mr. Chairman, I have one last question, if I
15 could.

16 The issue of a BNRT -- and I'd be interested
17 in the response of any of you who have been working a lot
18 on this -- the BNRT has been talked about as looking and
19 feeling a lot like a value-added tax. And oftentimes,
20 the reference is made to the European Union as perhaps
21 the broadest market where that applies, and that there's
22 not so many applications of this in the United States.
23 One of the reasons it's been talked about in the
24 literature, is that you need a -- there's a real value,
25 if you will, in having cross-market uniformity, for

1 example, in the European Union or throughout the United
2 States, among and between all the states, if they had
3 such a thing.

4 That causes me to ask the question of, when you
5 look at the European Union, one of the arguments that's
6 been made historically in the European Union for having a
7 value-added tax, is that they also have a very healthy,
8 robust social-service network, a social-service system
9 below it. And so those are often linked in the
10 literature. And California has just gone through, of
11 course, a pretty serious dismantling of at least some
12 portions of the social safety network in California due
13 to the budget issue.

14 I'm wondering if that issue came up at all
15 during your discussions about the -- again, oftentimes,
16 the parallel is drawn to the European Union, but there
17 is two component parts to that conversation, typically.
18 And I'm wondering if that was at all of issue to you or
19 it came up during your discussions?

20 Thank you, Mr. Chairman.

21 COMMISSIONER COGAN: Fred, that's a very good
22 question.

23 And I guess I'd say, it did come up, but really
24 in the context of volatility. I think we've all seen
25 what the volatility has resulted in for a lot of social

1 programs that people care about -- for education. And
2 the connection then is having a more stable revenue
3 source would prevent those kinds of dislocations, and
4 those kinds of cuts that we've seen in the last six to
5 eight months in California.

6 So I think it's in that connection that the
7 real gain in terms of social programs from a BNRT is
8 stability and as a way of avoiding the traumatic cuts
9 that we've seen in the recent months. And so I think
10 that's the connection.

11 Not so much in the European connection. I think
12 the Europeans, they fund an awful lot of their social
13 welfare programs through a payroll tax, in addition to a
14 BNRT. But I do think it's very important when we consider
15 the relative benefits of a BNRT, we think about it in the
16 context of what happens to social programs when we have a
17 highly volatile revenue source.

18 COMMISSIONER KEELEY: One last question about
19 that -- oh, I'm sorry, Chris.

20 COMMISSIONER EDLEY: Can I just -- I just want
21 to add. The other thing, frankly, that was on my mind,
22 and maybe it's the sixth reason why I favor the BNRT, my
23 sense is that because of the broad base, because it's a
24 broad measure of -- a much broader measure of economic
25 activity, that I think this is going to grow over time,

1 it's going to produce revenue over time as the economy
2 grows more reliably than the income tax, but especially
3 more reliably than the corporate income tax.

4 Now, that said -- and I hope none of the
5 Republicans here heard that, when I said that --

6 CHAIR PARSKY: We closed our ears.

7 COMMISSIONER EDLEY: Jennifer's point, I think,
8 is a really interesting one, that if, optimistically, we
9 think that there's going to be kind of a secular shift
10 away from consumption towards savings which, you look at
11 the public-sector deficits and you look at the unfunded
12 pensions, you've got to hope that something of that sort
13 is going to take place -- it's that kind of an argument
14 against the BNRT as a long-term growth in revenue.

15 And I'd certainly -- don't quote me on this,
16 but I kind of defer to economists' views on that, if I
17 get to pick the economist. But I could imagine an
18 argument also that to the extent that if there's more
19 saving, less consumption, that that would also have an
20 impact on corporate profits and perhaps on employment
21 levels.

22 So given all of that uncertainty, I still would
23 sense that the broader measure of economic activity is
24 going to produce better for us over the long haul.

25 COMMISSIONER KEELEY: My very last, last

1 question would be this: When you folks were wrestling
2 through the issues and you came up with -- and I think --
3 I like that what you did on the issue of volatility is
4 that you did, I think, fairly reflect the two schools of
5 thought or belief systems in play on the Commission:
6 One which says that volatility can be addressed through
7 dealing with the income tax, and another school of thought
8 here on the Commission is, volatility can be dealt with
9 through a rainy-day fund. And so you did both. Because
10 I think those are belief systems. There's not a right or
11 wrong. It's a belief system issue, which is the way you
12 would want to go about dealing with that. And I
13 appreciate it.

14 I was wondering if the following idea got
15 debated and, if so, what you all thought about it? And
16 I suspect we'll have a little bit of a debate about this
17 either later today or on Monday. But one way to look at
18 that volatility, the belief system I have, is that you
19 would leave the personal income tax alone; you would make
20 the changes you're suggesting in the State Constitution
21 relative to a much more aggressive rainy-day fund and not
22 give every legislator and the Governor the combination to
23 the lock that they could use anytime they chose to. But
24 also that within that, that what you could do over at the
25 personal income tax, is that you could treat capital gains

1 somewhat differently. Because we currently, as you all
2 know, treat it as ordinary earned income.

3 And I wonder if you discussed the idea, for
4 example, put more reliance on the rainy-day fund, don't
5 do much with the personal income tax, except as it relates
6 to capital gains; and maybe there, do something like this
7 take the capital-gain obligation and spread it out over
8 two or three years, when somebody has an obligation like
9 that, and say, "We'll try to flatten out that one-time
10 revenue spiking into the system," and causing more
11 volatility on the upside of the business cycle by, for
12 example, saying for two or three or four or five years,
13 you can take that one-time obligation you have and spread
14 it out. Maybe there is a pooled-money interest rate that
15 you would pay as a taxpayer, whatever the State
16 Treasurer's earning, something like that.

17 But did something like that come up? Was that
18 a part of the discussion?

19 Thank you very much. That really is my really
20 last question. Thank you.

21 CHAIR PARSKY: John, I'll let you comment.

22 But there's no question but that that
23 possibility has been thought about and discussed
24 throughout the Commission period.

25 But, John, do you want to make some comments?

1 COMMISSIONER COGAN: Just a couple comments,
2 Fred.

3 I think the gain in reduced volatility that
4 comes from focusing on the capital gains -- I can't
5 remember what the precise number was, Mark and Phil, but
6 as I recall, it was relatively modest. And I'd be
7 concerned about -- as much as I favor this rainy-day
8 fund, I'd be very, very concerned about whether it alone
9 can do the job or whether it could do 80 percent of the
10 job.

11 We have an awful lot of experience at the
12 federal level, we have a lot of experience at the state
13 level, across the various states with these types of
14 institutional mechanisms designed to prevent a legislative
15 body from spending money that they have. And I can't
16 think of one that has worked consistently over time at
17 the federal level or at state levels to prevent the kind
18 of volatility that we need to prevent if we're going to
19 deal with this problem of ratcheting up and ratcheting
20 down government spending.

21 So my view, just as one commissioner, is I like
22 the idea of a rainy-day fund, but I don't think we should
23 bet the ranch on it. And in some sense, that's what we'd
24 be doing if we left the income tax code in place.

25 COMMISSIONER EDLEY: And I'd just say that I've

1 raised these issues a couple of times. And you just
2 heard the sort of unreasonable intransigence that I
3 faced every single time that I raised the issue. But I
4 think also in the full group, raised the issue of
5 income-averaging of some sort once or twice, and it fell
6 like a lead balloon, so...

7 CHAIR PARSKY: Well, I will say that we did
8 hear testimony that doesn't take into account what you
9 just said about capital gains. But we did hear testimony
10 about the magnitude of the reserve that would be necessary
11 if we just went the route of the rainy-day fund and we
12 experienced the period we've experienced.

13 And I think the estimate was that about
14 30 percent -- 25 to 30 percent of the general revenue
15 fund would have to be reserved in order to deal by itself
16 in that. And maybe that would be acceptable to some, but
17 I don't think that's -- I think the conclusion was, that's
18 not practical. And so that's the evolution of the
19 thinking. Let's try to deal with both and not bet
20 everything on the rainy-day fund, but recognize that
21 changes in the personal income tax to accomplish these
22 objectives can't solve the problem, either.

23 COMMISSIONER BARRALES: Mr. Chairman?

24 CHAIR PARSKY: Okay, Ruben?

25 COMMISSIONER BARRALES: I've just got a couple

1 questions.

2 First of all, I do want to thank the three
3 amigos for all your work on that.

4 CHAIR PARSKY: Did you get that, from "whacky"
5 to "three amigos"? Write that down up there.

6 COMMISSIONER BARRALES: But also to Fred and
7 Richard, I know you both have done a lot, and have your
8 proposals as well.

9 And in all of those proposals, there is
10 something for everyone, I think, to oppose, and then
11 there are a few things that we might want to support as
12 well in all of these.

13 I've got two questions. One relates to the
14 inevitable question that we'd all have on the business
15 net-receipts tax is, it's labeled as a "tax on labor."
16 And what I'd like to do is kind of get on the table what,
17 you know, is the perspective there. And also to help me
18 think through -- and this is part of the same question --
19 how does this new system help or how does it aid
20 California's competitiveness in the 21st century and
21 moving forward?

22 There are a lot of competing interests in terms
23 of trying to put something together -- less volatility,
24 revenue neutrality, and all that. And I'm just -- I'm
25 struggling with, how does this new system make our state

1 any more competitive than the current system?

2 And so I'd appreciate your thoughts on that.

3 And then I might as well throw in my second question, and
4 this will be it.

5 Why not -- and I've come 180 degrees on this --
6 but why not, instead of a brand-new tax that's kind of a
7 value-added tax, kind of not, or the one that people are
8 familiar with -- why not lower the rate on the existing
9 sales tax, broaden the reach of the existing sales tax,
10 and approach the system from that perspective?

11 COMMISSIONER COGAN: So, Ruben, let me take that
12 one at a time and focus on the labor question. I think
13 it's a very good question. It's one that we heard from
14 the business community over and over again.

15 Isn't this a tax that would result in a
16 disincentive to hire workers? Or as Chris once put it:
17 Hire robots instead of people.

18 And I think where people come from is they say,
19 "Look, you're getting to expense your capital equipment,
20 but you don't get to deduct your labor compensation and,
21 hence, you've created disincentive." And it turns out
22 that that's just not so.

23 One way to think about it is that --

24 COMMISSIONER EDLEY: That's a lie.

25 CHAIR PARSKY: Now, now. Not from the gallery,

1 no matter what.

2 COMMISSIONER COGAN: So maybe the way to think
3 about it, Ruben -- and Mike might want to chime in on
4 this as well -- but the value of that deduction that's
5 lost for labor is, every dollar of labor expense, now you
6 lose 4¢ that you would have had if the BNRT rate is
7 4 percent, a deduction that you would have had, right, 4¢.
8 And so the value of the deduction lost is 4¢ on each
9 dollar for labor.

10 On capital, as it turns out, you're going to be
11 paying the BNRT when you purchase some capital equipment.
12 Because the BNRT taxes the labor, if you will, that went
13 into the creation of that piece of capital equipment.
14 And so the price of capital reflects, as does the price
15 of labor, the BNRT creating no tendency to substitute
16 towards machines and away from labor.

17 And I think the reality of it is that what
18 these value-added taxes do that economists like, is that
19 they place all of the inputs of production on a common
20 tax basis, and that's why people support it.

21 Why is it good for California? The answer I
22 could give you is that, look, you're taking a state that
23 has the highest corporate tax rate, 8.8 percent, and
24 you're knocking that down, we hope, down to just over
25 4 percent.

1 We think that that change in the tax rate is
2 going to be more than sufficient to make California a much
3 more attractive place for businesses to do business.

4 We think that the greatest deterrent to economic
5 activity is the tax rate that we apply to success. And
6 by getting that tax rate, by cutting it in half on
7 success, we think we're going to attract a lot more
8 successful businesses to California. So that would be my
9 answer.

10 COMMISSIONER EDLEY: Well, the only thing I'd --
11 I was going to say something about the sales, but also I
12 think a way that I think about the labor issue, as I'm
13 sure you could imagine was a major concern of mine, is
14 that when I, as a firm, buy the widget that I need in
15 order to produce washing machines, and I buy the widget,
16 the workers who constructed the widget, those wages are
17 not going to be deducted by the widget manufacturer.
18 But the value that's added by that labor -- the economic
19 input of that labor into the widget is going to be
20 deducted by me when I buy the widget as a business input.

21 So in that sense, the tax system, as a whole,
22 is, in fact, allowing a deduction for the contribution
23 of labor to the production.

24 The other thing I'd add is that with respect
25 to the capital, on the one hand, it is expensed when it

1 comes in, when I buy it, a piece of equipment, but I don't
2 get a deduction for the depreciation, which you do under
3 the income tax. And, of course, when I sell the used
4 piece of machinery later on, the revenue gained from the
5 sale of that used piece of equipment is included in my
6 tax base. And I'll pay a BNRT on any gain that I get
7 from selling that -- depreciated now -- that used piece
8 of equipment. So I think it sort of works -- I am
9 confident that it works out, and I don't think it skews
10 things away from labor at all.

11 The alternative that you mentioned regarding
12 the sales tax, I think it's very, very important that
13 everybody keep in mind that it's either the BNRT or the
14 status quo or expanding the sales tax to cover services.
15 And the difficulty with expanding the sales tax to cover
16 services, even if you lower the rate, is, you'll remember
17 from our plenary discussion, that when you look at that
18 list of services that would have to be included, the
19 politics of that are daunting, but then also the revenues
20 produced by the sales tax after you deduct business inputs
21 simply aren't as rich as what we get from the BNRT base.

22 Do you guys have that handy? But we lose a
23 substantial amount of revenue from expanding the sales
24 taxes, expanding the sales to services when we deduct
25 business inputs.

1 MR. IBELE: That's true. I don't have the
2 exact figures with me.

3 COMMISSIONER POMP: If you tax a new service,
4 you can't lose. You don't tax business inputs, but you
5 can't lose revenue.

6 COMMISSIONER EDLEY: No, but I'm saying, in
7 other words, by allowing the deduction for the business
8 inputs, you lose about 30 percent of it overall, so --

9 COMMISSIONER POMP: But if you tax a service --

10 CHAIR PARSKY: Wait, let's take it one at a
11 time.

12 I think that one point is, if you felt that the
13 taxation of business inputs under the current system is
14 a policy that you don't think is a good policy, and so
15 part of a change would be not to allow a deduction --
16 don't change to services for the moment, just allow a
17 deduction or a reduction in business inputs, not taxing
18 it twice, it would reduce the revenue that's created by
19 the current tax system by about 50 percent.

20 Now, extending the sales tax to services, if
21 you could extend them to all services, would increase the
22 revenue. But the policymakers of California have failed
23 continuously to do that.

24 COMMISSIONER EDLEY: The bottom line is, we
25 can't see a scenario in which expanding the sales tax

1 would generate enough revenue to do what we would like
2 to do in terms of PIT reductions and the corporate income
3 tax reductions.

4 CHAIR PARSKY: Mike -- I'm sorry, go ahead,
5 John.

6 COMMISSIONER COGAN: Ruben, one additional
7 thing, though, that Chris has said, when you extend the
8 services tax, the retail tax to services, if you exempted
9 the business-to-business sales, you'd be exempting an
10 awful lot of service activity. And that's one other
11 reason why the revenue gain from that extension turns out
12 to be quite modest.

13 COMMISSIONER EDLEY: And federal deductibility?

14 COMMISSIONER COGAN: Yes, one of the other
15 things is that if you extend this retail sales tax to
16 services, and you don't exempt business-to-business
17 transactions, you will get a lot of revenue. But a lot
18 of that will come from cascading of tax upon tax. And
19 that's a worry, and it's avoided by the BNRT.

20 COMMISSIONER BOSKIN: And the greater reliance
21 on the sales tax would reduce the -- it would cause a
22 federal tax increase for Californians because the
23 nonbusiness sales taxes are generally not deducted,
24 whereas virtually all of the BNRT would be.

25 CHAIR PARSKY: Okay, two more commissioners

1 have questions: Richard and then Curt. And then there
2 are two members of the public that made a special trip
3 here. I just want to give them an opportunity to speak,
4 and then we'll break.

5 Richard?

6 COMMISSIONER POMP: What time are you planning
7 to break, Gerry? Because I'm not going to be here Monday.
8 I've made a special trip here every meeting. That's three
9 days: One day out, the meeting, one day back. And so I
10 would like to be able to get my questions on the table,
11 so...

12 CHAIR PARSKY: Okay, well, we'll let you go with
13 your questions.

14 COMMISSIONER POMP: That's fine. I'll start
15 then so we don't waste any more time.

16 COMMISSIONER EDLEY: Or you could go first after
17 the break.

18 COMMISSIONER POMP: I could go first after the
19 break. That's fine, too.

20 CHAIR PARSKY: We have on our schedule to make
21 sure we get through the rest of the tax package that we
22 are due to discuss.

23 And I would say, Richard -- and I appreciate
24 all the questions. You have a lot of expertise. We did
25 hold a special conference with you and the staff to go

1 through a number of your questions. And so I hope that
2 that was informative. And I'm happy to have you repeat
3 every one of them. But I hope that was informative to
4 give you an idea of what this tax is.

5 But please proceed.

6 COMMISSIONER POMP: I'll start after lunch.
7 So let's make sure our public speaker gets heard.

8 CHAIR PARSKY: Okay, Curt?

9 COMMISSIONER PRINGLE: Again, I apologize for
10 not being here, but, in fact, Mr. Chairman, I spoke
11 extensively with you over the last couple of days, so
12 I think I understand some of what has been presented, as
13 with my conversations with Mr. Cogan and others.

14 I am very positive towards the package as it
15 moves forward. And a couple of the things that I think
16 are important to put on the table is, Fred references his
17 legislative service quite often, and I will just share
18 the fact that I have served longer in the Legislature
19 than Fred. And I may not have as complete of memory, but
20 I do remember the 5 percent across-the-board tax cuts
21 that Governor Wilson proposed in 1995 and 1996. It was a
22 5 percent reduction, both on the corporate rate, as well
23 as the personal income tax rate.

24 Some may wonder whatever happened to that
25 5 percent cut. It was provided for business, and it

1 wasn't provided for individuals, mainly because the
2 Democrats in the Legislature opposed the personal income
3 tax cut and accepted the bank and corp. tax cut. One of
4 those weird dichotomies that if you step back and look
5 at it, I think we now, through this process, seeing the
6 full element of all of the tax policy, may not necessarily
7 make those types of decisions, but there's still the
8 political, philosophical contradictions that are out
9 there.

10 But at that time, there were very few people
11 arguing in the Legislature for the personal income tax
12 cut, and there were plenty that were arguing for a
13 corporate tax cut. And I do think that, you know, from
14 my perspective, I want to share that I don't think that
15 we should beat around the bush. That, at least through
16 the direction of this package, there has been a shifting
17 of the taxpayer obligation in this state from a
18 broader-based tax base to the individual. And there's an
19 emphasis within this package of shifting that obligation
20 back from the individual to business.

21 I am a good card-carrying conservative
22 Republican; and I am not ashamed, embarrassed, or
23 concerned about that. But I also know that when I get
24 multiple letters from the business community, I understand
25 why, because there is a shifting from the individual's

1 percentage burden of what they are obligated to pay, both
2 on the personal income tax and sales tax, which we're
3 dramatically reducing, to a business net-receipts to fill
4 that hole. And I can accept that. I understand that.
5 But I also want to make sure that we hear, in context,
6 that we don't have a cavalcade of individual taxpayers out
7 here to come forward as representatives of individuals to
8 say thankfully, finally, since -- be it 1995 or ten years
9 before that, when other personal income tax reductions
10 were presented -- they've really not had that level of
11 personal income tax reduction.

12 But I do believe that part of our challenge
13 today and maybe Monday, when all of you meet, will be to
14 contemplate the biggest decision, and that is changing
15 elements of the tax code to this extent: What if we're
16 wrong? And I know right before I walked in, I checked
17 with Jennifer, and I know there was some brief discussion
18 of making sure we set up a system by which we are checked,
19 and that there is a backstop put in place as the phase-in
20 occurs to establish some entity by which there could be
21 a review to ensure that we didn't miss something or that
22 the unintended consequences, the action, or the burden to
23 business may be too great, or the burden to individual
24 industries may not have been calculated.

25 And I do want to make sure, Mr. Chairman, as

1 I've told you before, I'm really concerned about having
2 this review board established in our report after three
3 years of the phase-in implementation. We stop, we preset
4 who we think should be on it in terms of making sure it's
5 partisanly balanced; that we do get a chance to ensure
6 that some of these challenges that we've placed to our
7 staff today, challenges to determine what the tax rate
8 and the tax policy are in eight years, that, in fact,
9 we can reassess in a couple, to see if that actually has
10 played out. And if there is a terrible mistake, there for
11 that moment in time, things can be relieved and backed
12 away from that.

13 I think our tax policy today has many elements,
14 the tax code has many elements of terrible mistakes.
15 And that's why every year there are hundreds of bills
16 introduced in the Legislature to modify our tax code.
17 So for some reason, people to think we propose a grand,
18 sweeping package, that nothing will ever happen to it
19 again, is silly. That the tax policy we have today,
20 many of the things that have caused many of the problems
21 have been the changes that have been instilled by the
22 Legislature during my legislative service, and certainly
23 during Fred's, but also decades before that and decades
24 after.

25 So to somehow think that everything we do has

1 to be perfect today and it will never be checked and
2 there will never be a process or there will never be a
3 modification, that's just not the case.

4 So, one, I'd like to put it in here so that
5 there is a chance for that review. And I think that is
6 to our ultimate value.

7 And finally, I'll say that I would like to
8 suggest, even though I like the concept of a business
9 net-receipts, I would like to ensure that it doesn't get
10 over a certain level. And I personally hit that level
11 at about 4 percent.

12 So as we start phasing this in, if we get to
13 that 4 percent in terms of this annual recalibration and
14 we can't eliminate all of the state sales tax by the end
15 of the phasing in, when we hit the 4 percent BNRT, I don't
16 have any problem with leaving behind a percent or a
17 half percent or 1½ percent or whatever that may be,
18 because that is part of the definition of "revenue
19 neutrality," isn't it? That when we really do know the
20 value of this tax, that we are ensuring that it is
21 revenue-neutral, and we do stop at a point. And if we
22 leave behind at that point in time, the sales tax would
23 be the only other element of the pooled reductions that
24 would be catching that increase in the BNRT. If we leave
25 behind a portion of the sales tax, to me, I would feel

1 comfortable with that in a process of phasing in.

2 And finally, as a local elected official,
3 Ruben, one of the biggest challenges I think we all will
4 have, if there is a contemplation of expanding sales tax
5 to service, is what it will look like in this state. I
6 think I shared at a previous meeting. But every single
7 city in the state of California would have to vote to
8 expand or add a sales tax to services. The state can add
9 a sales tax to service and they can do that statutorily.
10 There's no constitutional restriction on that. That
11 could happen. But to make sure the rate of the -- the
12 rate in Orange County right now is 8¼ percent for a
13 purchase of a car. If you went to get a new set of tires
14 at your car dealer, if the City of Anaheim didn't impose
15 their local sales tax, the tax on the tires would be
16 8¼ percent, but I would have to have a two-thirds voted
17 by the city council and a two-thirds vote of the public
18 to impose that sales tax on service. So it would be
19 7¼ percent for that car dealer to pay on the service to
20 put on my tires.

21 But the County of Orange has a half-cent sales
22 tax for transportation. Every county, every self-help
23 county in this state would have to revote and authorize.
24 Otherwise, you would have varying tax rates by one
25 provider of service, a car dealer in this case for putting

1 on new tires, you'd have varying tax rates from city to
2 city, county to county. You would have potentially
3 hundreds of tax rates that could apply.

4 COMMISSIONER BARRALES: You have that now with
5 sales tax rates in different counties.

6 COMMISSIONER PRINGLE: Yes, the only difference
7 you have today in California is the ability the
8 Legislature gave to counties to raise the sales tax for
9 specific purposes. So, yes, from county to county. But,
10 in fact, a city to city, neighboring cities, all
11 individual votes, 435 cities in California would each be
12 required to have a two-thirds vote, or else they would
13 have a staggering sales tax within their city -- within
14 their city, and within the retailer within their city,
15 would have to have two separate logs as to what is for
16 services and what is for goods. Those are the complicated
17 challenges of a system that we also need to ensure is
18 simple enough so people understand, let alone the business
19 community that's being asked to collect that tax.

20 CHAIR PARSKY: Thank you.

21 I know everyone is waiting for a break.

22 Let me suggest that we ask Carl Morehouse and
23 Chris Norby, who have patiently waited here and I know
24 are a part of the City Council of the City of Ventura --
25 and the supervisor -- is that right? -- and vice-chair, to

1 make public comment. And then we'll take a break for a
2 brief lunch.

3 MR. MOREHOUSE: Good afternoon, Mr. Chair.

4 Okay, am I on now?

5 CHAIR PARSKY: You're on.

6 MR. MOREHOUSE: Okay, great.

7 Thank you, Chair and Commissioners for
8 accommodating us for this time. I will tell you this
9 chafes against my egalitarianism because all these other
10 people have been waiting patiently to testify, and I
11 apologize to them, as if my time was any more important
12 than theirs.

13 However, I think it's a perfect segue to step up
14 behind the last comments by Mayor Pringle. I come before
15 you as wearing many hats. I am the immediate past mayor
16 of the City of Ventura and a current council member. I
17 sit on the Ventura Council of Governments, on the Local
18 Agency Formation Commission, I formerly sat on the Ventura
19 County Transportation Commission; but most importantly, I
20 come to you today in my capacity as a regional council
21 member representing the cities of Fillmore, Ojai, Santa
22 Paula, and Ventura on the Southern California Association
23 of Governments where I chair the policy committee for the
24 community and environmental and housing development, of
25 which I am in front of you as specifically a chair of a

1 subcommittee of that.

2 Throughout the formation of the Senate Bill 375
3 by President Pro Tem of the Senate, Darrell Steinberg --
4 I will, by full disclosure, also tell you I'm a practicing
5 land-use planner, and I'll be going to the State Planning
6 Conference, which will begin this weekend -- as one of
7 these things that chafes at us. Throughout the formation
8 of 375, the intent was to try to link land use and
9 transportation, a very prudent idea for those of us who
10 are in the planning profession.

11 The one part of the component that he purposely
12 left out, and I understand why, was he forgot the fact
13 that every city has to pursue, as you are seeing here
14 with yourselves, a form of revenue stream, and that is
15 driven to the fiscalization of land use.

16 There is not one elected official, I believe
17 anywhere, who would be happy to build the housing that is
18 required by the State Department of Housing Development,
19 and add more constituents to scream at them on a meeting
20 night for money, when they're hunting for money to pay
21 for the ones that are already screaming at them. So the
22 process is, we tend to build big box stores, retail
23 outlets. And many of you have read in my deputy mayor
24 Bill Fulton's book, *The Reluctant Metropolis*, where he
25 talks about "Sales Tax Canyon" in Ventura.

1 After beating that gong for some time, I was
2 able to convince many of my peers on SCAG to form a
3 subcommittee to do the very kind of thing you've been
4 doing: Analyze the problems with the revenue stream,
5 particularly as it relates to the fiscalization of land
6 use.

7 I've been fortunate to have as my vice-chair
8 Chris Norby, who has already come and testified in front
9 of you in April.

10 Now, again, to show bipartisanship, we are not
11 only in different parties and have pretty strong feelings
12 in the similar vein, but he also was a county supervisor
13 and I'm a representative of the city.

14 So the Fiscalization of Land Use Committee met
15 a couple of weeks ago, and they've asked me to quickly
16 read into the record for you the conclusions from that
17 committee that they want to forward to you and present
18 to you also: A Conceptual Framework for Local Government
19 Finance Reform. Because the one thing we want to remind
20 you as you go through your deliberations, is please keep
21 in mind that every citizen in the state of California
22 resides in a city, the 485 cities referenced by the mayor,
23 or the 58 counties.

24 So very quickly, if I may.

25 *"On behalf of the Fiscalization of Land*

1 *Use Subcommittee of the Southern California*
2 *Association of Governments, I enthusiastically*
3 *applaud the Commission on the 21st Century*
4 *Economy's efforts at stabilizing, modernizing,*
5 *and rationalizing state and local government*
6 *revenue.*

7 *"We've reviewed your current draft proposal*
8 *and are supportive of its general direction and*
9 *many of its tax policy concepts. We urge the*
10 *Commission, however, to consider the*
11 *implications of any reform package on local*
12 *government finance. It is at the local level*
13 *where so many valuable services are delivered*
14 *and where government meets the people. A focus*
15 *of local government finance is in keeping with*
16 *the Commission's mandate to suggest changes to*
17 *state and local revenues that will result in a*
18 *revenue stream that is more stable and*
19 *reflective of the California economy.*

20 *"Examination and explanation of the*
21 *local implications of the proposed business*
22 *net-receipts tax will be especially important.*

23 *"SCAG's Fiscalization of Land Use*
24 *Subcommittee is made of local elected officials*
25 *from around the Southern California region,*

1 *home to roughly half of the state's population.*
2 *We've been evaluating various fiscal reform*
3 *concepts with the goal of providing more*
4 *stability and fairness to local government*
5 *revenue. As our name suggests, we are*
6 *particularly interested in confronting the*
7 *fiscalization-of-land-use phenomenon and*
8 *removing the perverse incentives that the*
9 *current system of local government finance*
10 *creates for land-use planning and development*
11 *in our communities.*

12 *"To encourage more balanced development*
13 *and an end to the chase for sales-tax dollars,*
14 *we've studied a range of reform options and*
15 *have developed a framework for reform that*
16 *would allow cities to voluntarily exchange*
17 *some of their sales tax revenue stream for a*
18 *greater share of local property taxes. This*
19 *would incentivize the full spectrum of land*
20 *uses rather than the current bias towards*
21 *retail development.*

22 *"We also believe a split-roll adjustment*
23 *to the property tax law allowing periodic*
24 *reassessment of commercial properties should be*
25 *considered by the voters.*

1 *"I've also submitted a memo summarizing*
2 *our reform framework for further information.*
3 *The reform concept SCAG is pursuing appear to*
4 *be compatible and consistent with the direction*
5 *of your commission. The objectives of our*
6 *respective efforts could not be more*
7 *complementary. I hope that we can work together*
8 *as the ideas we have exchanged evolve from*
9 *concept to legislation.*

10 *"Thank you again for your efforts in*
11 *serving the people."*

12 Let me just put on a very personal note. I've
13 watched with great interest as a student of public
14 administration and political scientist, your deliberations
15 up here. I know how difficult they are. And I laud you
16 in your efforts, and I hope that you can continue. And
17 thank you, and may the good Lord provide you with the
18 wisdom for coming up with a very good recommendation.

19 Thank you for accommodating my time.

20 CHAIR PARSKY: Thank you very much.

21 MR. NORBY: Far from waiting patiently,
22 Mr. Chair, we've been fascinated and grateful that those
23 such as you are engaged in this policy effort.

24 Oftentimes, in programs like this, it's the
25 staff talking to each other and those on the committee

1 sort of nodding heads and then wanting to put a final
2 imprimatur on this. But we're thankful for this process
3 and we're excited by it at SCAG. We're looking at local
4 government revenue, trying to defiscalize it.

5 I reported to you at Davis. We looked at a
6 number of proposals you've been chewing on. But the one
7 that we have, which is the most politically palatable,
8 has not to do with sales-tax sharing, which I originally
9 thought was where we were going to do, but then you have
10 to fight with the high and low sales tax cities, even if
11 you even it out just in terms of doing the growth.

12 But allowing cities voluntarily to give up all
13 of their local sales tax revenue -- not lower the tax,
14 but give up the revenue to the State in exchange for a
15 higher percentage of their property tax. Trade it one
16 for one. And then the city isn't worried about the big
17 boxes. The city is not incentivizing retail. In fact,
18 the city values all of its property taxpayers, including
19 residents, equally.

20 And this is the one that we're focusing on.
21 Now, we're still talking about sales-tax sharing, we're
22 still talking about the split roll. I personally don't
23 think that's a good idea or it's necessarily going to
24 happen. But the allowing of cities to voluntarily do
25 this, I think would have a profound effect on local

1 government. It's something that the Legislature could do
2 without a vote of the people. It wouldn't allow any tax
3 increases. It would allow simply the way that local
4 government relates to land use by equalizing revenue and
5 defiscalizing it.

6 Thank you.

7 CHAIR PARSKY: Thank you all very much.

8 MR. MOREHOUSE: Finally, as a reminder, let me
9 quickly hand out city pins for the City of Ventura so you
10 all know and remember in the back of your mind about local
11 governments.

12 CHAIR PARSKY: I'm not sure any of the
13 commissioners will get any more than that through this
14 process. So take your pin here.

15 We're trying to -- it's two o'clock now. Let's
16 take a 30-minute break, come back. We are going to offer
17 Richard Pomp a chance for further questions. Then we
18 need to move to a discussion of the pollution tax and a
19 discussion of the royalty on potential oil drilling. And
20 then we'll try to come back around and see where we are.

21 Thank you.

22 COMMISSIONER BOSKIN: How long?

23 CHAIR PARSKY: Thirty minutes.

24 *(Midday break 2:00 p.m. to 2:50 p.m.)*

25 CHAIR PARSKY: We'd like to start now. And what

1 we're going to do is, Commissioner Pomp is the last
2 questioner for this part of the tax package that we've
3 been discussing. And then we'll turn to several other
4 elements of the package that I'd like to come back around
5 and get a sense from the commissioners where they are in
6 their thinking, and then we'll see where we go from here.

7 So, Richard, why don't you proceed with
8 questions?

9 COMMISSIONER POMP: Yes, thank you, Gerry.

10 I've got a bunch of questions, I think -- and
11 this is going to be a judgment call for you. I think if
12 we stop after every question and have people give an
13 answer, it may run a little longer than what you want.

14 I've had the benefit of sitting next to John
15 at lunch, and that was very useful. That will help
16 short-circuit some of the questions I have.

17 So if you're happy with that format, I'll just
18 put stuff on the table. And then afterwards, people can
19 respond or not.

20 And I think, for the record, as long as we're
21 doing a mea culpa, I am not a registered Democrat, so..
22 I'm not even -- not of any kind.

23 Let me start with two fallacies that I think
24 are very important to clear up. One is, just because a
25 certain income group pays the lion's share of a tax, it

1 does not follow the tax is progressive. That's a
2 fallacy. I can have a regressive tax; and if I have so
3 many wealthier people than poor people, they will still
4 pay the lion's share, even under a regressive tax. So
5 you can't use that to look at progressivity or
6 regressivity.

7 The second fallacy: What we are talking about
8 the NBRT has nothing to do with Europe. Europe has what
9 is known as a "credit invoice transactional value-added
10 tax." It is a retail sales tax collected in stages.
11 That is not what we are talking about here. There's only
12 one country in the world that arguably has something
13 similar to what we're doing here, and that's Japan. It's
14 not even clear it's similar. So that's the second point.

15 The European experience, when everyone is in the
16 system, as is true in the economic union, the world looks
17 very different from the world we are debating here where,
18 with the exception of Michigan, we're going to be the
19 only state with an NBRT. That does put our vendors at a
20 competitive disadvantage. When they buy things and pay
21 an NBRT and then export it, the single factor means they
22 won't pay any NBRT on the sales proceeds received on the
23 export, but they will have NBRT embedded in the cost of
24 the good that's being exported. They will compete in the
25 U.S. market with everyone from other states that do not

1 have this tax.

2 This is why there is value in having a tax
3 system that's not out of step with other states, and
4 that's why I really am somewhat skeptical about our
5 eliminating the corporate income tax, a tax we've had for
6 about 70 years; a tax that 90 percent of the states have;
7 and a tax for which we have not heard any empirical data
8 has negative consequences on the California economy.

9 Now, maybe the basic reason it doesn't is that
10 very few corporations pay it. I'd like to know more about
11 that. I've proposed a plan that has at least the
12 potential of turning that around.

13 But I want to rehabilitate and reinvigorate the
14 corporate income tax. I would never give up a tax that's
15 part of the mainstream of the U.S. economy. I think
16 that's a big mistake.

17 Marginal tax rates. In general, sure, I
18 subscribe to the philosophy that a lower marginal tax
19 rate is better than a higher one. That debate has
20 basically occurred in the context of the federal system,
21 where you have rates approaching, with the phase-outs,
22 50 percent. And people don't appreciate -- I'm sure
23 people on the Commission appreciate it because they
24 probably pay it. But, you know, what Congress did, rather
25 than raise nominal rates, was take away our personal

1 exemptions or itemized deductions, you throw on the AMT,
2 and you could easily be pushing 50 percent. That's a
3 debate --

4 CHAIR PARSKY: Rich, I don't mean to interrupt,
5 but if you could separate your remarks. You'll have an
6 opportunity to make statements, but just separate your
7 remarks from questions that we have the staff --

8 COMMISSIONER POMP: This is a question, but the
9 staff is not going to be able to answer it.

10 CHAIR PARSKY: Okay.

11 COMMISSIONER POMP: Is there any evidence that
12 the marginal tax rate of the California income tax has
13 had ill effects on the economy?

14 And you can answer this by introspection, Gerry.
15 You're very hardworking. Are you going to work any harder
16 if we lower your marginal tax rate? I'd doubt it. I
17 mean, I just can't believe it. I can't believe other
18 people on this panel will work harder. So I'm a little
19 skeptical about what we're going to get in return from
20 lowering marginal tax rates.

21 My question is, is there any evidence? And
22 I'll leave that one for people to deal with.

23 But I have a combination of comments --

24 COMMISSIONER PRINGLE: Mr. Chairman, I would
25 like you to answer his question: Would you work harder?

1 CHAIR PARSKY: Well, it's hard for me to assess
2 that issue in connection with the pay I am receiving for
3 this commission. If it was taxed at a little higher rate,
4 I might work a little bit less. But given that, I'm not
5 sure -- Richard, I would only say to you that I thought
6 at several commission meetings you, as a commissioner,
7 said that, among other things, that lowering the rates
8 and expanding the tax base were positive things that you
9 could see happening in California. And that was a
10 statement you made. I don't know quite how you would
11 implement that, but I'd be interested.

12 COMMISSIONER POMP: Implementing is no harder
13 than what you're thinking about implementing or we're
14 thinking about implementing with the NBRT.

15 I would eliminate waste and inefficiency. I
16 might start with tax expenditures that can survive a
17 cost-benefit analysis.

18 If we agree that something should be eliminated
19 because there is no empirical support that it does
20 anything that overcomes the loss in revenue, I would use
21 that revenue, and I would be happy to lower the rate of
22 that particular tax.

23 COMMISSIONER EDLEY: Are you reading any news
24 coverage of what happens in Sacramento? In what universe
25 do you think the State Legislature would do what you're

1 suggesting?

2 COMMISSIONER POMP: The same universe that's
3 going to say they're not going to do the NBRT, so you
4 could read the politics the way you want and I'll read it
5 the way I want. But I would like to at least talk about
6 what the right answer is. You know, there's plenty of
7 room in the Legislature to play, "Let's make a deal."
8 I'd like to talk about what the right answer is. I think
9 we should be role models on this commission. And you
10 could go ahead and read whatever the politics are that
11 you think they are. But we're not going to get anywhere
12 debating politics.

13 CHAIR PARSKY: Let's just focus on questions.

14 COMMISSIONER POMP: Right.

15 Next question: Half of the reduction in the
16 personal income tax, which is about seven or seven and a
17 half billion dollars, goes to about 3 percent of the
18 taxpayers.

19 And I guess my question is, was that in order
20 to reduce volatility or is that a combination of reducing
21 volatility and hoping to get some favorable incentives
22 built into the personal income tax so people would invest
23 more in California or work harder and things like that?

24 And, you know, for me, that's a very skewed
25 distribution, half to 3 percent of the taxpayers. I'd

1 like to know why. I'd like to know why the itemized
2 deduction for medicals was eliminated, as well as the
3 child-care credit. I mean, I don't really understand.

4 We have an R & D credit that we're proposing in
5 the BNRT, a credit for which at least -- I don't read
6 politics, I read the economic literature and empirical
7 studies. And I find that there is no empirical evidence
8 that the R & D credit pays for itself. So we're willing
9 to do something for which there's no empirical evidence
10 and we're eliminating a child-care credit. I mean, I
11 don't understand that kind of trade-off, and I don't
12 understand -- and I did listen to the President's speech
13 last night. It's hard for me, in the light of that
14 speech, to understand how we are eliminating an itemized
15 deduction for medicals. People who are losing jobs or
16 losing medical benefits and are no longer covered by
17 insurance; they're paying for stuff out-of-pocket. I
18 don't understand how we're not taking that into account.

19 I would like to see, along with the additional
20 data that others have asked for, I'd like to see the
21 winners and losers in each of these income groups.
22 Because I am curious how many of the losers ends up
23 paying more tax under this proposed system -- and we know
24 there will be some -- are going to do that because of the
25 elimination of the medical deduction and child-care

1 credit. And that should be knowable.

2 So I also have trouble thinking about this whole
3 package without knowing the incidence of the NBRT. And
4 I know it's tricky and I know we also had a consultant
5 who gave us some best guesses as to the incidence effect.
6 And I believe about 70 percent was going to have the
7 incidence of a sales tax.

8 Working with that, I would like to see sort of
9 the omnibus incidence effects. I have trouble thinking
10 about one part of that. And I appreciate John's remarks
11 about how may we know more about one tax than the other.
12 But nonetheless, I'd like to at least see our best
13 estimate, perhaps using our consultant's prediction that
14 it will have the effect, the NBRT, at least to the degree
15 of 70 percent as a sales tax. And so I'd like to see what
16 that does.

17 We're reducing the tax on the wealthy, which is
18 going to be the largest-growing sector when the economy
19 turns the corner. This has been true in all other periods
20 of time. We are moving to a consumption tax which, with
21 the difficulty of obtaining debt financing, we're seeing
22 a falloff in consumption. The Feds are likely to move to
23 a consumption tax to finance the deficits and health care.
24 They're going to be squeezing consumption, would be at
25 least my guess. It seems to me, it's sort of the wrong

1 time to be eliminating a corporate income tax.

2 Profits grow very fast as you come out of a
3 recession. So we are eliminating a tax on a fast-growing
4 revenue base; we're cutting taxes on the wealthy, a
5 fast-growing revenue base; and we are moving to what is
6 likely to be a slow-growing revenue base. That just
7 doesn't make good sense to me.

8 I'd also like to know -- and this is for the
9 staff -- this is easily knowable -- how did they grow
10 income from current year to 2014? Was the same growth
11 factor used for each income group?

12 And that, I suppose, is an easy "yes" or "no."

13 MR. SPILBERG: The way that income was grown
14 was by basically form of payment. So there were capital
15 gain growth rates, there were wages and salary growth
16 rates and the other sources of income. And because those
17 sources of income are distributed differently across the
18 distribution, you would have different growth rates across
19 the distribution.

20 COMMISSIONER POMP: So a higher growth rate was
21 used for capital gains than for wages?

22 MR. SPILBERG: Yes, it was.

23 COMMISSIONER POMP: Okay. And, again, let me
24 add my compliments to everyone else's kudos for the
25 enormous work of the staff, including the drafting of a

1 bill -- or at least some parts of a bill, though I
2 understand we're not going to propose that, and I don't
3 know how we could vet it -- but an enormous amount of
4 work went into that.

5 One of the things I worry about, Gerry, with the
6 NBRT: When it comes to an income tax, the Legislature has
7 a pretty good idea of what the right answer is. If I come
8 in and I'm lobbying; and I say, "Oh, you know, vacation
9 should be deductible because I can show you evidence it
10 increases productivity," a legislator may consider that,
11 but they will at least know it's not part of the structure
12 of an income tax. You don't give a deduction for personal
13 consumption like vacations.

14 There is no one who understands what the
15 normative structure of the NBRT really should be. And I
16 am sure debates that our working group had indicate, in
17 many cases, you just don't know what the right answer is:
18 Financials, insurance. It's difficult -- nonprofits.
19 And I am just afraid that while we might like something
20 that's theoretically pure, it is going to come out like
21 Swiss cheese out of the legislative process. People are
22 going to come in and they're going to go, "Look, this is
23 really unfair to labor. You don't get a deduction for
24 labor. You've got to do something about it." And I'm
25 willing to bet you something will be done about labor.

1 Now, we heard some sophisticated arguments
2 about how labor really isn't treated more favorably than
3 capital purchases. The premise of those arguments was
4 that the producer of the capital good was subject to the
5 NBRT. That is a European argument, where you can be
6 somewhat assured that in a large economic union, the
7 provider will be subject to the NBRT, or what's
8 equivalent, the transactional value-added tax.

9 There is no assurance here. California is going
10 off on this on its own.

11 If I go over to some other state, buy capital
12 equipment, put it in my truck, bring it back to
13 California, I don't believe that the supplier of that is
14 subject to the California NBRT.

15 COMMISSIONER EDLEY: That's a risk.

16 COMMISSIONER POMP: It's a risk -- I think it's
17 more than a risk. It's a risk I think I would take on a
18 contingency basis. I mean, if someone comes to me --

19 CHAIR PARSKY: You'll be paid the same amount
20 of money you're getting for serving on this commission for
21 that.

22 COMMISSIONER POMP: Well, until we win it,
23 that's right.

24 If someone comes to me in Connecticut and asks
25 for an opinion letter on the NBRT and I do all my services

1 in Connecticut and then I e-mail them or Fed Ex them or
2 fax them the results of my services, I don't believe I am
3 an NBRT payer, and I don't believe any known theory of
4 economics nexus makes me an NBRT payer. If that's true,
5 everyone going to --

6 CHAIR PARSKY: Well, let's just pause on that
7 for a minute. Let's just pause.

8 COMMISSIONER EDLEY: Yes.

9 CHAIR PARSKY: Because I'd like Carl to just
10 talk about the work that was done by the Franchise Tax
11 Board in preparation of a memo relating to the
12 constitutionality -- of potential constitutionality.

13 COMMISSIONER EDLEY: Gerry, I think that what
14 Richard just said is unexceptional in terms of the
15 applicability. The question is, how many transactions of
16 that sort would actually occur.

17 He's just saying, there wouldn't be any
18 economic nexus if all the business takes place in
19 Connecticut. I think that's clearly true.

20 The question is, how many people would drive
21 across state lines in order to consummate the deal and
22 thereby get out from under it? And I think it would be
23 a trivial fraction.

24 COMMISSIONER POMP: Most people call me and
25 don't drive, so very easy to call today.

1 COMMISSIONER EDLEY: Frankly, I'm less worried
2 about you than I am about --

3 COMMISSIONER POMP: Than Nevada.

4 COMMISSIONER EDLEY: Nevada, yes, exactly.

5 COMMISSIONER POMP: And then we -- the NBRT --

6 CHAIR PARSKY: Let's just -- Carl, make a few
7 comments here.

8 MR. JOSEPH: Okay. Well, we were asked by the
9 Commission to do some work in that area about what the
10 possibilities are, about the constitutionality of an
11 economic-presence-type nexus standard. And we reviewed
12 the cases that have been decided -- at the state level,
13 mind you. It's never been at the Supreme Court. And,
14 you know, we came to the conclusion that it's most likely
15 that this is okay.

16 Now, granted, bad facts can make for bad law.
17 And one transaction with you, Richard, on the service
18 contract in Connecticut would probably not be the case
19 that ends up in front of the Supreme Court.

20 Nonetheless, if you had a taxpayer who was
21 providing services of a significant quantity to California
22 taxpayers and was availing themselves of the California
23 market, I think that, at least the cases at the state
24 level have indicated a rather strong prevalence on the
25 state's part, that there is no physical presence necessary

1 to apply the tax.

2 COMMISSIONER POMP: And the key phrase
3 was "availing themselves of the California market." I
4 don't think Carl is suggesting I avail myself of the
5 California market when I sell to a customer who takes a
6 good, picks it up in a truck, and brings it back to
7 California.

8 Are you suggesting that's availing myself?
9 If so, everyone's availing themselves of the California
10 market. Anyone who sells inventories to a California
11 purchaser, who comes and loads it up on a truck and
12 goes --

13 CHAIR PARSKY: Okay, Richard, Richard, Richard.

14 COMMISSIONER POMP: So, all right.

15 CHAIR PARSKY: Richard, hold on. Let's -- you
16 went through all of these questions in a conference call
17 with the staff.

18 COMMISSIONER POMP: But not with the
19 commissioners.

20 CHAIR PARSKY: I know. It's okay.

21 COMMISSIONER POMP: So what difference does it
22 make?

23 CHAIR PARSKY: I'd like you to try to focus on
24 some issues here that bother you, and then let the
25 Commission know whether or not you would support, in any

1 form -- any form whatsoever, with any conditions attached,
2 an exploration of a business net-receipts tax or not.

3 COMMISSIONER POMP: The issue of nexus is the
4 900-pound gorilla in the room, Gerry. I mean, that is
5 the -- you're either going to have an incentive for
6 offshore outsourcing or you're not.

7 And the fact that I express these same views
8 with the staff, that's not the same thing as sharing them
9 with the commissioners.

10 So let me -- in the interest of time, you know,
11 how to think about nonprofits. You can't just say they're
12 treated this way under an income tax and, therefore, we're
13 going to carry over that treatment to a value-added tax.
14 You have to start from thinking about what a value-added
15 tax means. You can't just assume that the correct
16 treatment under an income tax follows into a value-added
17 tax.

18 NOLs --

19 CHAIR PARSKY: Just pause on that.

20 You would tax nonprofits under a BNRT?

21 COMMISSIONER POMP: I did not say that. I'm
22 saying --

23 CHAIR PARSKY: Well, what are you saying?

24 COMMISSIONER POMP: I'm giving you a thought
25 process of how to think about it, that --

1 COMMISSIONER EDLEY: We did. We did. And it's
2 a hard question. We came up with a recommendation. Tell
3 us what you think would be a better recommendation.

4 COMMISSIONER POMP: I was not privy to your
5 discussions, so -- but I will say this: I know what the
6 wrong answer is. The wrong answer is to assume that what
7 we do in the income tax is the right answer under a
8 value-added tax.

9 COMMISSIONER EDLEY: It wasn't an assumption.
10 It was the sense that -- I'm sorry, it wasn't an
11 assumption, Richard. It was a sense of, well, the
12 Legislature has clearly made a decision that a certain
13 class of activity is going to have tax-favored status.
14 And even though this is a different form of tax, we were
15 kind of thinking what would be more consistent with the
16 previous policy judgment's balances that were struck in
17 the Legislature. And at least what John and I thought,
18 and I think Gerry agreed, that you could do on the one
19 hand, on the other hand; but we thought that the better
20 of the argument was, if the Legislature wanted to favor
21 them under Tax System A, the Legislature would probably
22 also prefer to favor them under Tax System B. And as a
23 policy matter, it could go either way. So that was our
24 reasoning process.

25 I'd love to be educated, though.

1 COMMISSIONER POMP: Here's my initial starting
2 point: I may decide under an income tax that the concept
3 of income has no rigorous meaning when applied to a
4 certain kind of activity -- maybe a charitable activity,
5 do I count donations as income, are they gifts which are
6 traditionally exempt under an income tax? I might decide
7 that the notion of income doesn't apply to a nonprofit
8 and, therefore, I will exempt it from a tax on profit.

9 That doesn't mean that a nonprofit doesn't
10 generate value-added. It may or may not. You know,
11 that's a debate worth having. What kind of nonprofit?
12 What are they doing? Are we going to be discriminating
13 between a for-profit provider of that good or service
14 and a nonprofit provider of that good or service? Those
15 are legitimate questions to have.

16 All I'm suggesting is, an answer under an
17 income tax doesn't necessarily carry over.

18 COMMISSIONER EDLEY: I think that's absolutely
19 right. But I think that we may have a disagreement on
20 the conceptual clarity behind section 501(c) of the IRC.
21 I don't think it's all about confusion about what is or
22 isn't income.

23 COMMISSIONER POMP: Well, it may not be totally.

24 COMMISSIONER EDLEY: Right.

25 COMMISSIONER POMP: All right, that's fine. I

1 agree, it may not be all about that. All I'm suggesting
2 is, when you move to a different kind of tax base, one
3 has to rethink these from scratch.

4 NOLs -- when you think about an NOL in the
5 corporate income tax, what does the NOL say? The NOL
6 says that, "I will shelter a future amount of income
7 from taxation, equal to the NOL."

8 If we're going to eliminate a corporate income
9 tax, the system has kept its promise. Not only have we
10 sheltered an amount of income from taxation equal to the
11 NOL, we've sheltered all income from the NOL.

12 We've kept our promise. There's no logical
13 reason why that NOL should be carried over into a
14 completely different tax, a value-added tax.

15 COMMISSIONER EDLEY: Here would be the logic:
16 The logic would be that anytime one constructs a
17 transition strategy in moving from one tax structure to
18 another tax structure, part of it is about logic, part
19 of it's about a sense of what's equity, and part of it
20 pays attention to what are people's reliance interests.
21 Part of it is a concern about a disruption in markets,
22 et cetera.

23 And I think putting all of those things
24 together, it's not just a matter of logic, it's a notion
25 that you have firms that have been constructed with a

1 certain expectation about stability in the tax system
2 and what it's going to look like, and they may have
3 expectations about having an asset on their books that
4 will be valuable if they're acquired by another
5 corporation, et cetera.

6 And while it doesn't seem reasonable to try to
7 preserve 100 percent of all of that value, nor does it
8 seem to me reasonable to think that it should simply
9 evaporate with the adoption of a different tax structure.

10 So, again, I think that this is a matter of
11 just trying to reach some agreement about what's a
12 reasonable way to strike a balance as you're trying to
13 craft a transition between, from one system to another.

14 COMMISSIONER POMP: And I guess the way to test
15 that theory is, if we were just to eliminate the corporate
16 income tax, without any kind of financing mechanism that
17 could be tied to it, like the NBRT -- we just decided in
18 a flush time to eliminate the corporate income tax, would
19 the State really be thinking of reimbursing people for
20 NOLs which they have gotten the benefit of and that there
21 will be no future income -- all income to be taxed?

22 COMMISSIONER EDLEY: I absolutely think the
23 State would think about it. As to whether or not they'd
24 actually do it, I'd have my doubts simply because it would
25 be far less practical in a situation in which taxes were

1 disappearing, I mean, whatever planet that is.

2 COMMISSIONER BOSKIN: Well, it would have been
3 nice if we were convened during a period of robust
4 revenues and we could have a tax cut along with a reform.
5 That would make everybody's life easier.

6 But I think, Richard, one of the main
7 differences between NOLs and other fluctuating income, is
8 that many businesses have extremely cyclical revenues and
9 extremely cyclical profits. Therefore, there will be
10 times they are negative.

11 We don't reimburse them. Our tax system is
12 asymmetric. It stops at zero, okay. It's unlike, my
13 income is X one year and 2X another. I may wind up in a
14 higher tax bracket, and there's an issue about whether
15 averaging ever made sense, et cetera. But if it's
16 "minus X" one year and "2X" the next year, and it's
17 averaging "X," I'm not being taxed on that. I never get
18 to take advantage of the fact that I had "minus X." I
19 should have gotten a refund on my taxes and I didn't.
20 It's being carried over.

21 COMMISSIONER POMP: So you're saying that if I
22 operate in a loss position for my entire history and then
23 go out of business, I'm entitled to a refund of the taxes
24 I never paid?

25 COMMISSIONER BOSKIN: No. No, no, no. There

1 has to be some practical limit, sure.

2 COMMISSIONER POMP: And finally, on the minimum
3 tax, I mean, if you really believe everyone should pay a
4 minimum tax, we, I think, are eliminating the minimum tax
5 on LLCs, corporations, and every other entity.

6 I happen to think there should be a minimum tax,
7 at least on business entities. I think in recognition of
8 their use of the infrastructure, there should be a minimum
9 tax. And I don't understand the logic of eliminating it.

10 COMMISSIONER BOSKIN: But not on people?

11 COMMISSIONER POMP: People, I think, is a little
12 harder because we have an ability-to-pay notion when it
13 comes to people.

14 And I also think there's something more subtle
15 with work, that minimum tax will be collected through
16 withholding. And most people become completely oblivious
17 to taxes collected through withholding.

18 And what the focus groups show -- and you can
19 do this through introspection -- most people know the
20 refund they got from the IRS and they know the check they
21 wrote when they sent in their return, they are
22 hard-pressed to tell you what the total amount of their
23 personal income tax was actually paid over the course of
24 the year, so -- and I have a feeling this would be the
25 same thing with people.

1 COMMISSIONER EDLEY: Do you have a sense of,
2 if there were a minimum tax, what it should be?

3 It's currently, what, \$800?

4 MR. JOSEPH: Yes.

5 COMMISSIONER EDLEY: \$800 on the bank and
6 franchise tax?

7 COMMISSIONER POMP: I would just continue it.
8 People are used to it, so...

9 Anyway, Gerry, I have more, but I could see no
10 one has patience.

11 CHAIR PARSKY: Well, Richard, let me just say
12 this: I know that you have a lot of experience in these
13 areas, and I know that you've proposed an alternative way
14 to look at what the Commission should do.

15 Inherent in what you have suggested, I think --
16 although part of the text of what you've suggested
17 included an open mind with respect to the BNRT and an open
18 mind in terms of adjusting the personal income tax rates.
19 But it sounds like your mind is closed -- and that's
20 perfectly okay, you're welcome to, and should, carry
21 forward your own personal views irrespective of whether
22 the rest of the Commission reaches consensus.

23 Just so that everyone understands, your
24 approach, I gather -- tell me if I'm wrong -- would be
25 to leave the personal income tax all alone? Don't touch

1 that tax?

2 COMMISSIONER POMP: No. As my memo suggested,
3 I can certainly accept, in the interest of trying to
4 reach a consensus, a distributionally acceptable
5 reduction. 50 percent of the reduction to 3 percent to
6 the taxpayers is not acceptable to me.

7 CHAIR PARSKY: No, no, I was just reading from
8 the summary of your plan --

9 COMMISSIONER BOSKIN: What about the taxes that
10 are already being paid? They're paying 50 percent of the
11 taxes.

12 COMMISSIONER POMP: Yes.

13 COMMISSIONER BOSKIN: So we're keeping the
14 distribution of the tax burden the same, basically.

15 COMMISSIONER POMP: And you're giving half of
16 the about \$7 billion reduction to 3 percent of the
17 taxpayers.

18 COMMISSIONER BOSKIN: Who pay half the income
19 taxes.

20 COMMISSIONER POMP: And I've suggested that the
21 percentage someone pays of the total tax does not address
22 the distributional issue. I could --

23 CHAIR PARSKY: Well, we just have a disagreement
24 about that.

25 COMMISSIONER POMP: You're talking of more

1 wealthy people.

2 COMMISSIONER BARRALES: Can I ask, Mr. Pomp,
3 what would your proposal be? How would you distribute
4 that?

5 COMMISSIONER POMP: I don't see -- I mean, I
6 have heard no testimony, no evidence -- I don't think
7 the Commission has heard any -- that there are negative
8 consequences from the existing personal income tax in
9 California.

10 COMMISSIONER BOSKIN: Charles McLure, James
11 Hines, and Roger Gordon all testified to the high marginal
12 tax rates in California, personal and corporate, being a
13 disincentive to invest in, expand businesses in, locate
14 in California, and were one source of California's
15 competitiveness problems which were part of our charge.
16 They are the second and third items of our charge by the
17 Assembly and Senate leaders and the Governor.

18 Now, research --

19 COMMISSIONER POMP: If you notice --

20 COMMISSIONER BOSKIN: I totally agree that when
21 you try to pinpoint a study just of California, it becomes
22 a needle in a haystack. That becomes very hard.

23 COMMISSIONER POMP: And I cited studies, Gerry,
24 in my memo, about how marginal rates had no effects in
25 these other --

1 CHAIR PARSKY: Your memo has been distributed
2 to the public. The public has your memo.

3 I was trying to understand as a commissioner
4 what it is you're asking this commission to do in response
5 to their charge. And it sounds like -- it sounds like
6 you don't have a plan for changing the personal income
7 tax. That wasn't one of your seven points.

8 COMMISSIONER POMP: That is correct. I accept
9 that.

10 CHAIR PARSKY: Okay, I just wanted to make sure
11 we've got it clear, so everybody understands.

12 COMMISSIONER POMP: But I do not have a closed
13 mind to something that is more distributionally
14 acceptable.

15 CHAIR PARSKY: No mind is ever closed
16 permanently.

17 COMMISSIONER POMP: Of course.

18 CHAIR PARSKY: No mind.

19 The points that you raise in your memo, however,
20 that relate to the corporate income tax -- and there are
21 several -- in terms of provisions that you thought were
22 included, that were not appropriate by the California
23 Legislature, and the publishing of the names of publicly
24 traded corporations who received expenditures, as well
25 as the publishing of the names of corporations that paid

1 the corporate tax -- all of those suggestions would be
2 unnecessary if we eliminated the corporate tax.

3 COMMISSIONER POMP: Not the tax expenditure
4 one.

5 CHAIR PARSKY: Well, on the tax expenditure, I
6 think we've made it clear that our charge was not to deal
7 with expenditures. But I would just like to ask you the
8 question: Would you want to identify tax expenditures
9 under the personal income tax as well?

10 COMMISSIONER POMP: I might. You know, John
11 and I were talking at lunch. Put us in a closed room,
12 we'll come up with a list of tax expenditures that we
13 think are worth --

14 CHAIR PARSKY: Okay, I think everyone --

15 COMMISSIONER BOSKIN: Would you also like to
16 list every Californian that is exempted from the income
17 tax?

18 COMMISSIONER POMP: Individuals have a right to
19 privacy that corporations that are publicly traded, that
20 file voluminous SEC reports, do not have. And that's why
21 my proposal was limited to publicly traded corporations.

22 CHAIR PARSKY: Okay, listen, you have a lot of
23 expertise. You're perfectly entitled to your views. I
24 think everyone understands the direction you would like
25 to go.

1 If, between now and September 20 you decide to
2 go in a different direction, I'd like you to let all the
3 commissioners know, because we are still seeking unanimity
4 around this table. But it's clear that the direction that
5 is being outlined is not a direction you'd like to go in.

6 I would only urge that you look at, extensively,
7 the magnitude of work that's been done, and that you
8 listen to the balance of the presentation that is going to
9 be made by Commissioner Keeley and Commissioner Boskin,
10 and see if, out of all of that, you can find your way to
11 support a proposal by all the commissioners that isn't a
12 take-it-or-leave-it proposal, but is an attempt to be at
13 reform and a request of the Legislature to take this
14 effort seriously.

15 COMMISSIONER EDLEY: I'm sorry, Gerry, can I
16 just ask a question procedurally? I'm very interested in
17 supporting three of Richard's recommendations. That
18 regarding a severance tax, the independent tax court, and
19 ending the pay-to-play.

20 At what point would you propose that we talk
21 about those --

22 CHAIR PARSKY: Two of those: The independent
23 tax court and the pay-to-play concept is part of our
24 discussion today, and will be one of the potential
25 recommendations for this commission. It was identified

1 as part of the tax package earlier.

2 COMMISSIONER EDLEY: Right.

3 CHAIR PARSKY: And it will be.

4 The severance tax issue will be also addressed,
5 but I think in the context of -- and I'm not quite sure
6 I understand exactly what it would apply to -- but it
7 will certainly -- this severance tax, do you want to
8 explain that a little bit?

9 COMMISSIONER POMP: Yes. It is, I think, in
10 use by every state in the country that has substantial
11 natural resources. By severing it, it is the bringing of
12 the resource to the surface. It differs from the royalty
13 proposal of Michael, but it's similar in that it applies
14 to natural resources.

15 There have been bills filed in the past in
16 California that are a very good starting point for this.
17 The Commission would have to decide what a good rate
18 would be. But the groundwork has been done. I didn't
19 repeat in my memo, but the groundwork's been done.

20 CHAIR PARSKY: We'll discuss that in the context
21 of Michael's -- yes.

22 COMMISSIONER LOZANO: I have one question also.

23 CHAIR PARSKY: Yes.

24 COMMISSIONER LOZANO: The comment about the
25 deductions -- and I do recall in one of our commission

1 meetings, we talked about medical benefits -- medical
2 care. And could you describe for us why that was not
3 included in our package?

4 CHAIR PARSKY: Well, we started with the notion
5 that there would be no deductions. That's one starting
6 point.

7 I think Richard commented that he would favor
8 that, that there would be no itemized deductions at all.
9 Start just with AGI. And discussion around the table was
10 that that wasn't something that the entire Commission
11 could coalesce around. And so we started down the list of
12 things that could be included in itemized deductions.

13 I think -- my recollection is that it was the
14 property tax, in effect, taxing a tax, was something that
15 a number of commissioners said didn't make sense.

16 And then we identified, and for the last two
17 Commission meetings had on the table, these three itemized
18 deductions. That's not to say that the medical deduction
19 isn't available at the federal level, because it still
20 would be -- and child care and a number of other things.
21 And it is important not only to look at these tax
22 proposals as a package, but also see the interrelationship
23 between the changes made here and the federal tax, which
24 we will certainly comment about.

25 But I thought that there was the ability to

1 achieve full consensus, but including only those items.

2 COMMISSIONER POMP: They were all deductible
3 at the federal, so that doesn't distinguish the medical
4 from any of the others.

5 COMMISSIONER EDLEY: What was the revenue loss
6 associated with the health-care deduction? Do you guys
7 remember?

8 CHAIR PARSKY: I think -- did we identify the
9 revenue loss relating to the health-care deduction?

10 COMMISSIONER EDLEY: I remember, way back
11 earlier we did.

12 CHAIR PARSKY: I think earlier, we did.

13 MR. IBELE: I don't recall. I can check the
14 transcript.

15 COMMISSIONER POMP: It just seems to me, Gerry,
16 it looks very callous on our part to take away a
17 child-care credit, deduction for medicals, and leave a
18 charitable, for example. And that just, I don't think,
19 sells well.

20 COMMISSIONER BARRALES: I thought we weren't
21 supposed to do medical?

22 COMMISSIONER POMP: I wouldn't have any of
23 them. As Gerry correctly stated, I certainly would
24 prefer moving the AGI. But if we're not going to do it,
25 then I don't understand the line we're drawing.

1 CHAIR PARSKY: Okay. Let's --

2 COMMISSIONER HAUCK: Gerry?

3 CHAIR PARSKY: Bill?

4 COMMISSIONER HAUCK: It's pretty clear to me
5 that I erroneously relied on our meeting going from
6 eleven o'clock until four o'clock today. I mean, I have
7 an obligation I've got to see to.

8 We also have a number of people, according to
9 what you've said, who would like to address this
10 commission; and I'd like to hear them. So what I'd like
11 to suggest is that we let those people make whatever
12 presentation they have to make. It's also clear that we
13 are going to have another meeting on Monday. And however
14 it proceeds, we could cover what we don't cover today as
15 we begin on Monday.

16 So I'd like to suggest that we hear from the
17 folks that have sat here all day, listening to this mostly
18 erudite discussion, so that they have an opportunity to
19 say what they would like to say.

20 CHAIR PARSKY: I couldn't agree with you more.

21 Okay, thank you all very much for this
22 discussion of this aspect of the potential set of
23 recommendations.

24 I would like to now turn to the balance of the
25 tax package identified that we were going to be

1 considering. And I want to remind everyone of the
2 framework, again, that we agreed would be included in
3 Sections 1 and 2, off of this specific two-page tax
4 package.

5 Let me just ask the commissioners one question
6 in connection with that. We did not hear, since the last
7 meeting, any individual commissioner with a presentation
8 or incremental additional work on the inclusion in
9 Sections 1 or 2 of the split roll. And so I would ask of
10 the commissioners if it would be acceptable to move that
11 item away from consideration within Sections 1 and 2,
12 which is what we're talking about.

13 Would any commissioner have objection to that?

14 *(No response)*

15 CHAIR PARSKY: Okay. Then that leaves us for
16 discussion the pollution tax, which I'd like to turn to
17 now, and introduce -- and have the discussion led by
18 Fred Keeley. And I know he has several people that have
19 supported putting this effort together. And we'd like to
20 have a full discussion of this.

21 COMMISSIONER KEELEY: Mr. Chairman, thank you
22 very, very much. I really appreciate it.

23 I would, by way of a piece of housekeeping
24 business, if members want to find this -- if
25 commissioners, rather, want to find this -- take a look

1 at Tab 9, and the next-to-last blue sheet of paper --
2 your next-to-last piece of blue paper in Tab 9, that
3 should start with a piece of paper that says, "Petroleum
4 Fuels Pollution Tax: Rationale and Process," if we're
5 all at the same place.

6 Okay, and what follows behind that is draft
7 legislation from Legislative Counsel on this matter.

8 So now I've got you focused on the item.

9 Let me frame this issue up this way; and if I
10 could, if I could ask Bill Dorey, the president and CEO
11 of Granite Construction to join us at the witness table,
12 and John Boesel from CalSTEP to also join us.

13 *(Mr. Dorey and Mr. Boesel came to the*
14 *witness table.)*

15 COMMISSIONER KEELEY: Okay, thank you.

16 Mr. Chairman and Commissioners, during the
17 course of our discussion and deliberations, we have
18 discussed the idea of a pollution tax or, as Mr. Dorey
19 always wants me to call it, a "green fee." So that sounds
20 a lot like golf, but I'm willing to do it, anyway.

21 The idea here is this: We have discussed this
22 idea, from time to time, and that is that California has
23 taken a lead in the nation, among all the states in the
24 United States, with regard to addressing the issue of
25 greenhouse gas emissions. And most significantly, through

1 the passage of Assembly Bill 32, and the passage and
2 enactment of Senate Bill 375. And what these said was
3 that California, irrespective of what the federal
4 government may or may not do, that California would put
5 itself in a position and make commitments to reduce its
6 greenhouse gas emissions to 1990 levels, and that it
7 would do it over a relatively short period of time. And
8 that the Air Resources Board and the California Energy
9 Commission and the Office of Planning and Research and
10 others in the executive branch would develop strategies
11 for dealing with that in accomplishing that emission
12 reduction. And they are working to do exactly that.

13 There is a considerable body of opinion which
14 says that in order to achieve those emission-reduction
15 goals, it will also be essential for California to price
16 the burning of fossil fuels at a level that will cause
17 two things to happen: One is a level of consumption would
18 be reduced; and secondly, that we would send a signal into
19 the marketplace that we are going to internalize the cost
20 of burning gasoline and diesel fuel, so that those costs
21 no longer fall onto the general public by way of public
22 health costs, reductions in agricultural productivity,
23 and so on. And that it would also send a signal that
24 California is the place where venture capital, together
25 with intellectual capital, together with entrepreneurial

1 spirit and risk-taking, would help move global
2 climate-change solutions to market. Whether that is
3 different types of fuel or different types of vehicles
4 or any other imaginable solutions, that one of the key
5 ingredients to making that happen is to price fossil
6 fuels appropriately so that the costs are internalized.

7 So the proposal in front of you has two
8 features to it that I'd like to draw to your attention.

9 First is, it is a tax. It takes the existing
10 excise tax on gasoline, which is 18¢ in California, which
11 was adopted in 1990, with no indexing for inflation. So
12 we have essentially lost the purchasing power of that 18¢.
13 It adds a new 18¢ to it, and then indexes that with growth
14 over the next ten years; so that we get to a place fairly
15 quickly where California has priced the burning of those
16 fossil fuels to cover the internalizing of the cost, to
17 price it to internalize those externalized costs we have
18 now; and secondly, to send essentially signals into the
19 marketplace that will start adjusting behavior.

20 That is one side of this proposal, and that is,
21 raise the excise tax, raise it for ten years into the
22 future.

23 The other side is, what do you do with that
24 money?

25 Now, I understand that, strictly speaking, the

1 Commission has steered away from wanting to get terribly
2 involved in expenditures. And I understand that.

3 Let me explain a couple of things about this.
4 To some extent, we cross that line a little bit in the
5 BNRT discussion and others, because there's places where
6 you're going to want a certain kind of credit here or a
7 certain kind of credit there. Well, those are
8 expenditures under budgeting.

9 This goes far beyond that. I understand that.
10 But here's the reason that it goes beyond that:
11 Article XIX of the State Constitution governs all of the
12 expenditure of this money -- all of the expenditure of
13 this money. It has to be any expenditure of any money
14 raised through the state excise tax on gasoline. It has
15 to be consistent, the expenditure has to be consistent
16 with Article XIX of the Constitution.

17 And so what the working group tried to do --
18 and we met on August 12th and had a lengthy agenda that's
19 in your packet. We again met on August 18th, and we again
20 met on August 25th. And it was a large group of people.
21 It was folks from the Assembly and Senate Revenue and
22 Taxation committees, the Speaker's office, the President
23 Pro Tem of the Senate's office, the Franchise Tax Board,
24 Board of Equalization, interested parties from the
25 business community, interested parties from local

1 government, from transit, from transportation agencies,
2 and so on.

3 And what we did was, we looked at the current
4 situation relative to underinvestment in California in
5 our infrastructure. And we said, if we are going to be
6 competitive in the 21st century, one of the things that
7 has to happen is that our transportation and transit
8 systems need to be as modern as our ideas are and as our
9 aspirations are.

10 Secondly, is there a way that, while raising
11 this tax, we can relieve some of the pressure on the
12 state general fund? And we found that the answer to that
13 is yes. There's about a half a billion dollars a year
14 right now, spent from the general fund to retire general
15 obligation funds approved by the voters for transit and
16 transportation.

17 We would propose to take the first half billion
18 of this and pay those bonds instead of general fund, thus
19 relieving a little bit of the pressure on the general
20 fund.

21 We also understand that AB 32 and SB 375 are
22 the law of California; and that, as a commission, we
23 should be pursuing the enforcement and the robust
24 enactment of those and realization of those aspirational
25 goals contained in those two measures.

1 So we have some funds that are consistent with
2 Article XIX of the Constitution that would be appropriated
3 for AB 32 and SB 375 compliant purposes. But the vast
4 bulk of the money raised -- and it would start at about
5 three and a half billion dollars a year, and by Year 10,
6 be somewhere up around \$13 billion to \$15 billion a
7 year -- the vast bulk of that would be split evenly
8 between State Caltrans appropriations -- we're not going
9 to micromanage that. The Legislature is not going to
10 micromanage that. They have a huge, billions and billions
11 of dollars of backlogged projects and maintenance and
12 repair and so on. This would provide a steady, dedicated
13 funding source to try to claw away at that backlog. And
14 so do local governments. They are responsible in the
15 City of Berkeley for maintaining all of their county
16 roads. In Santa Cruz County, we have 610 miles of county
17 road in the unincorporated area. I don't know what it
18 is in Anaheim, but it's a lot of city road. And they
19 have precious little resources to be able to maintain the
20 existing system, much less make improvements.

21 So the idea here is to really attack this issue
22 from two points of view using tax policy. One is the
23 pricing signals, and the other is the expenditure side,
24 consistent with Article XIX of the Constitution.

25 And the two folks that have been very kind

1 today to show up and provide some additional information,
2 first, I'd like to introduce Bill Dorey, who is the
3 president and CEO of Granite Construction. They're a
4 very large construction firm based in a very small town,
5 Watsonville, in Santa Cruz County. And Bill Dorey and
6 I have known each other for a very long time. And we
7 just talked two or three weeks ago about this topic.
8 And as Bill likes to tell anybody who will listen, he
9 thinks this is the first time he and I have agreed on
10 anything, so...

11 But Bill has a presentation, and then John
12 Boesel will have one, and then I'll introduce John in a
13 moment.

14 Thank you, Mr. Chair.

15 MR. DOREY: So do I have to keep pushing this?

16 CHAIR PARSKY: Unfortunately, I think so.

17 MR. DOREY: All right, Fred is right, my name
18 is Bill Dorey, and I'm the CEO of Granite Construction
19 Company. And we build roads, streets, dams, tunnels,
20 transit facilities from Alaska to New York City. We are
21 headquartered in a very unlikely place, and that's
22 Watsonville, California. There's about 30,000 people that
23 live there. That's where we started. Our California
24 contractor's license is number 89, to give you an idea of
25 how old this company is.

1 I have been absolutely fascinated by this
2 discussion today. I arrived at about eleven o'clock
3 today. I've listened to all the testimony. And I can
4 tell you, there are some very smart people dealing with
5 a very complicated question. And I am thankful that you
6 are all here, and I'm thankful that you've given me the
7 opportunity to testify.

8 I am not going to try to solve the tax-structure
9 problems which the state of California has.

10 CHAIR PARSKY: We would welcome that, if you
11 could do that.

12 MR. DOREY: I would not begin to be able to,
13 I think, weigh in on the task that you all have in front
14 of you. I am, however, going to trying to help you think
15 through transportation and the volatility and the
16 certainty that transportation does -- the volatility that
17 we don't need and the certainty that we do need from a
18 funding standpoint.

19 The work that we have done at Granite and the
20 work that we have done through Transportation California,
21 which is an agency who was very instrumental in the
22 passage of Proposition 42, as well as the Proposition 1B
23 bond, transportation bonds recently, the work that we've
24 done was entirely independent of what Fred has been doing.
25 And that's, I think, really the coincidence in this, to

1 some degree.

2 I realized what he was doing about three weeks
3 ago. I did call him and suggest to him that this is
4 probably the first time he and I had ever been in
5 alignment on any subject; that we ought to talk about
6 this. And what you will hear from Fred is, he is coming
7 at this, I think, largely from an environmental
8 perspective. And where I am coming at this, is a need
9 to build the infrastructure and maintain the
10 transportation system that we currently have and build
11 a system for the future.

12 Okay, so let's get right into this. California
13 is not investing adequately in its infrastructure. I
14 don't think that anyone would argue with that. All you
15 need to do is drive around this state and compare what
16 we have in California with what other states are doing
17 and have built, and I think you will conclude that we are
18 simply not doing that.

19 And I'm going to try to walk you through a case
20 for this. Not my words, certainly not Granite's words,
21 but words of commissions, like yours, that have dealt
22 with this problem at the state level and from third
23 parties that have weighed in.

24 California needs an additional \$3 billion
25 annually simply to address the maintenance and

1 rehabilitation of our system. This is from Caltrans.
2 This is their five-year and ten-year maintenance program.
3 This is what Caltrans is saying.

4 In addition -- and this is really startling --
5 transportation is woefully underfunded. California's
6 ten-year underfunded needs are currently estimated by
7 the Governor's Commission on Transportation to be
8 \$160 billion through a ten-year period.

9 And this finding occurred in 2005. And if you
10 were to ask Caltrans to update this number -- and I've
11 done this, by the way -- that number is roughly
12 \$200 billion today. So it's an enormous need. It's an
13 enormous need, and I think an enormous challenge that
14 we all have as Californians.

15 As Fred suggested, the tax on gasoline in
16 California was last increased in 1990. In 1990, it was
17 9¢ a gallon. It went from 9¢ to 18¢ over a period from
18 1990 to 1994, and has not been increased since then.

19 It's not indexed to inflation. So the public
20 record would indicate that it's lost a third of its
21 purchasing power since 1994. I would argue that it's
22 been a lot more than that, and it's simply inadequate
23 today.

24 And while this is the subject that I'm
25 intimately interested in and I believe I know something

1 about, it's a small part of the question that you all are
2 dealing with.

3 Proposition 42 is another funding source that
4 California depends on. It is a sales tax on gasoline.
5 And that is something that you all are dealing with. My
6 understanding is that the sales tax in the state of
7 California, you are contemplating eliminating that. If
8 that occurs, 8¢ -- roughly 8¢ a gallon that finds its way
9 through the general fund and back into transportation
10 will disappear. So there may be some very instrumental,
11 unintended consequences that would occur to transportation
12 funding if the sales tax is eliminated.

13 Now, I'm not suggesting that the sales tax
14 can't be eliminated. All I'm suggesting is, it needs to
15 be replaced. And, roughly, the equivalent would be about
16 8¢ a gallon.

17 Proposition 1B is the bond funds that were
18 passed recently --

19 COMMISSIONER PRINGLE: Excuse me, Mr. Chairman.
20 I need to clarify just one of those points, sir,
21 if I could.

22 MR. DOREY: Sure.

23 COMMISSIONER PRINGLE: Under Prop. 42, I
24 understand the sales tax for what you're talking about.
25 But you say 8¢ a gallon.

1 So it's not 100 percent of the state sales tax
2 that goes for transportation?

3 MR. DOREY: No.

4 COMMISSIONER PRINGLE: So what percentage --

5 MR. DOREY: This is a bit of a black box. And
6 I'm not sure that I can explain it entirely. Maybe Fred
7 can help mere.

8 COMMISSIONER PRINGLE: But maybe the staff
9 could?

10 MR. DOREY: But if you do the arithmetic - if
11 you do the arithmetic, at three bucks a gallon times
12 20 million gallons a year, it's \$60 billion times
13 5 percent, is \$3 billion. And only a billion and a half
14 of it is finding its way back into transportation. And
15 there's something called the "spillover funds."

16 Does that answer the question at this point?

17 COMMISSIONER PRINGLE: No.

18 Mark or Phil, could you tell me what I'm --

19 MR. IBELE: Let me see if we can get a
20 clarification on that, and I'll have to come back to it.
21 I don't have an immediate response.

22 COMMISSIONER PRINGLE: If you could get back to
23 me later in that discussion. Because under Prop. 42, all
24 the money of sales tax, the state's share, goes for
25 transportation. How it is --

1 MR. IBELE: Right. How it's divided between
2 local governments and the state.

3 COMMISSIONER PRINGLE: Right, that's the
4 question I need to have answered.

5 MR. IBELE: Okay.

6 MR. GENEST: Would you like an answer to that?
7 Because I happen to know that answer.

8 CHAIR PARSKY: Are you going to answer it?

9 MR. GENEST: Well, I probably know this answer
10 in more detail. He's correct. The spillover is, it's a
11 very complex mechanism. But it takes money that if it
12 wasn't for the spillover rule, would have gone into
13 Prop. 42. And it takes it before Prop. 42 is calculated.
14 So Prop. 42 is still 5 percent of the -- well, it's
15 currently 5¼ -- but it's 5 percent of the price of gas
16 per gallon, the price. And then that would all go into
17 Prop. 42, except some of it gets into this other mechanism
18 called a spillover, and that's why there's a differential.

19 But I would remind you, your proposal says that
20 you're going to eliminate the state sales tax that's
21 general purpose. And what I mean by that is, you're not
22 going to eliminate the sales tax on gasoline. And that
23 will continue to go to Prop. 42.

24 CHAIR PARSKY: Is that distinction understood?

25 COMMISSIONER PRINGLE: No, it's not.

1 CHAIR PARSKY: Okay, well, then say it one more
2 time, Michael.

3 COMMISSIONER PRINGLE: Nor was any of the other
4 part of his explanation.

5 CHAIR PARSKY: Let's take them in pieces.

6 COMMISSIONER KEELEY: Mr. Chairman, let me just
7 say, that this is the issue I raised this morning under
8 the BNRT, which is -- and asked as a placeholder that
9 you would address this, sometime we could deal with this
10 between now and Monday, which is, if you eliminate the
11 sales tax in its entirety -- and that's the proposal --
12 and replace it with the BNRT, then the sales tax on
13 gasoline would need to -- in order to preserve the
14 Prop. 42 funding, you would need to replace that somehow.
15 Now, you could either earmark --

16 CHAIR PARSKY: Explain -- it's a distinction
17 between the excise tax and the sales tax; is that what
18 you're driving at?

19 MR. GENEST: No, those are two separate taxes
20 here. But what we're talking about here -- at least
21 it's my interpretation of the written proposal that was
22 presented this morning, in those words where it says,
23 "Eliminate the general purpose sales tax at the state
24 level." I'm assuming that doesn't mean the sales tax as
25 it applies to gasoline, because that's tied up in an

1 initiative. You could not change that by statute. And
2 your proposal is supposedly just going to deal with
3 statutory changes, unless the one case where you're
4 putting it under the Constitution. But your tax proposal
5 was statutory only.

6 If so, you can't touch 42, so you can't
7 eliminate the sales tax on gasoline.

8 COMMISSIONER PRINGLE: Well, Mr. Chairman, I
9 would like to have a complete legal opinion on that
10 specific point, because I believe Prop. 42 talks about
11 the sales tax on gasoline. It doesn't create a separate
12 tax that is defined as a sales tax on gasoline. It
13 applies to the sales tax that is in the statute.

14 You just suggested, Mr. Genest, that it's gone
15 up to 5¼ percent, therefore, whatever the Legislature may
16 set as the tax rate, those dollars under Prop. 42 go for
17 a transportation account. But what if the Legislature
18 set, as a tax rate, at zero?

19 MR. GENEST: I think you're right. You could
20 actually -- I misspoke. You could actually eliminate the
21 entire sales tax. But my interpretation of the words
22 in the proposal, when it says, "Eliminate the state
23 general purpose sales tax," I was assuming -- maybe I'm
24 incorrect -- that you intended to keep the sales tax on
25 gasoline so that you don't interfere with the operation

1 of Prop. 42. Now, maybe I'm wrong for your intention.

2 COMMISSIONER EDLEY: I should speak for my
3 intention. My intention was to do whatever it is Curt
4 wants to do, if only I could figure out what that is.

5 MR. GENEST: Well, that would be what he would
6 want to do.

7 COMMISSIONER EDLEY: But, seriously, you want to
8 preserve that money going to --

9 COMMISSIONER PRINGLE: Yes, I do. I personally
10 want to preserve it. And I think that's what we're
11 hearing from all the transportation advocates.

12 But, Mr. Chairman, I'm not a lawyer. I might
13 be one of the few not here that's a lawyer. But I don't
14 believe what we just heard is correct. I believe that
15 Prop. 42 talks specifically about the sales tax that is
16 collected on gasoline, whatever the rate is that is the
17 state portion of the sales tax.

18 Prop. 42 did not redefine the sales tax on
19 gasoline as a non-general tax. That sales tax is still
20 the general tax applied to all commodities of purchase.
21 Therefore, I am concerned that, Mike, you may be reading
22 more into this; and I think the concern of the
23 transportation community is, in fact, that if sales tax
24 went to 20 percent, they would have a lot more money for
25 transportation. We're not arguing that. But if it went

1 to zero, they'd have no money for transportation. And
2 that's what their argument is.

3 MR. GENEST: I think it's a question of, what
4 does the proposal actually mean. You could do a couple
5 of things --

6 CHAIR PARSKY: I think we need to come back on
7 that. But let's, just so that I understand what, in
8 making the assumptions about the amount of revenues that
9 would be necessary to fill the general fund from
10 elimination of the sales tax, what did the staff assume
11 was happening with respect to the sales tax on gasoline
12 that presumably was dedicated?

13 MR. IBELE: We included the general 5¢. That
14 would include the sales of gasoline, too, within those
15 numbers.

16 Now, if you went in the direction of keeping
17 that dedicated portion, you'd have a business charging one
18 sales tax rate on gasoline sales, and non-gasoline sales a
19 different rate, which is one complication.

20 CHAIR PARSKY: But you assumed what Curt was
21 assuming, that --

22 MR. IBELE: Yes.

23 CHAIR PARSKY: -- in effect, that although the
24 words said, for purposes of the general fund, you assumed
25 that the sales tax, as applied to gasoline, as well as

1 everything else, would be gone?

2 MR. IBELE: Would be gone, that's correct.

3 CHAIR PARSKY: Okay, that clarifies it.

4 What the assumption was, it doesn't mean it has
5 to be the recommendation.

6 COMMISSIONER KEELEY: Understood.

7 So as we get back to Mr. Dorey, I'd like to,
8 again, request a placeholder on this question, so that the
9 existing sales tax on gasoline, which is how I understand
10 it is calculated, there is the price of the product, there
11 is the federal excise tax, there's the state excise tax.
12 You add those three up and apply the state sales tax to it
13 to decide how much per gallon; is that correct? Did I
14 do that right? So it's the price of the product, plus
15 federal excise, plus state excise, multiplied times the
16 state sales tax rate. And that generates the Prop. 42
17 funds.

18 MR. IBELE: That's correct.

19 COMMISSIONER KEELEY: Okay. So that issue we
20 have to continue to deal with sometime between now and
21 Monday.

22 Back to Mr. Dorey, because what we are talking
23 about, so members are clear about it, we are talking about
24 increasing the state excise tax. Not the sales tax. But
25 we do need to address this through your BNRT proposal.

1 Mr. Dorey?

2 MR. DOREY: Thank you.

3 And I think one of the distinctions between what
4 I'm here to talk about and what I heard from you all most
5 of the day is, this concept of revenue-neutral. I might
6 as well get this on the table. I'm not here to talk about
7 revenue-neutral. What I'm here to try to ask you to think
8 about, as we conceive this tax program, potential tax
9 program, that we address the need for additional funding
10 in transportation. And certainly, the first place to
11 start that is to keep from losing the current funding.

12 Proposition 1B was passed by the voters about
13 three years ago, and it was a bond fund that raises
14 about -- today, about \$4 billion per year.

15 The problem with Proposition 1B is, number one,
16 we have not been able to sell the bonds recently, so that
17 program is not working, and it will phase itself out in
18 about two or three years.

19 To put it into perspective with the other taxes
20 that fund transportation currently in California, it is
21 worth about 20¢ a gallon. So that's just a reference
22 point for you all.

23 Okay, so this is a busy slide. And I actually
24 thought about not including this. But I think it's
25 important because there's a lot of conversation today

1 about whether or not a tax on fuel or a fee on fuel is
2 something that's sustainable. So this is, once again,
3 Caltrans information. And if you look on the left side
4 of this chart, 2010, about 28 million registered vehicles
5 are in the state of California. And if you walk down that
6 same line, 15 years from now, it's expected there will be
7 36 million registered vehicles in California. And we
8 clearly need to prepare for that.

9 Vehicle miles traveled would go from 362 billion
10 miles in 2010, to almost 500 billion miles in 2025.

11 And here is where it gets interesting, and here
12 is where I think Fred may disagree with this, but this
13 is, once again, Caltrans information. It's probably
14 directionally close, and that is, that the average fuel
15 economy in 2010 -- including trucks, by the way -- is
16 about 18½ miles per gallon. It is not expected to
17 significantly go down. In fact, according to Caltrans,
18 it's going to stay pretty much the same. So fuel
19 consumption will go up over the next 15 years if you
20 believe Caltrans.

21 So I think the conclusion here is the user fee
22 will be a reliable transportation funding source for the
23 foreseeable future.

24 So this is, once again, a very busy slide. I'm
25 not going to spend a lot of time on it, and I'm not here

1 to advocate that we adopt a European-style taxing program
2 on fuel in this country. But I think it's important for
3 this commission to recognize what others are doing as it
4 relates to fuel taxes.

5 And this was out of the *New York Times*, 2008,
6 so it's a little dated; but I think the message is still
7 very, very appropriate. The United States, if you look
8 at the left side, that's price at the pump. In June of
9 2008, it was about 4 bucks. And you can look down that
10 line, on the left side, and see what fuel was costing
11 elsewhere around the world. It was in the neighborhood
12 of \$8.50.

13 The next line over is price excluding taxes,
14 \$3.51 in the United States, and basically about \$3.50
15 throughout the balance of the world. So that tax on fuel
16 in the United States is about 50¢ a gallon, compared with
17 about \$5 a gallon most everywhere else.

18 Taxing fossil fuels, rather than subsidizing
19 renewable energy sources, provides Americans with the most
20 incentive to reduce consumption and switch to another
21 fuel. And that's where Fred is coming from. I believe
22 that. I suspect we would not get an argument from anyone
23 on the Commission. It's pretty simple economics. And I
24 think we saw that in place when fuel got to \$4. People
25 all of a sudden, including me, were concerned about

1 something I hadn't been concerned with in some time, and
2 that was the efficiency of my automobile. So it's not a
3 bad thing. But I'm not here to talk about the
4 environment, I'm here to talk about transportation and
5 getting people efficiently from one place to another.

6 Having said that, I have chastised Fred a little
7 bit for his pollution tax slogan. I don't think it's a
8 pollution tax. I do think it's just about the greatest
9 tax you can come up with.

10 So let's talk a little bit about the economics
11 around raising fuel taxes -- or any kind of tax, for that
12 matter, to invest in transportation.

13 Once again, most of this information is from
14 an organization called TRIP, which is who CNN calls when
15 they want to get unbiased information about what it costs
16 the average motorist to deal with certain inefficiencies
17 in transportation.

18 CHAIR PARSKY: You're sure CNN looks for
19 unbiased information?

20 MR. DOREY: I don't know about that.

21 COMMISSIONER EDLEY: Gerry wants to know who
22 Fox calls.

23 MR. DOREY: I think they all call this. They
24 all call TRIP. TRIP is the authority.

25 CHAIR PARSKY: We have to lighten things up a

1 little bit. It's okay.

2 MR. DOREY: I appreciate that.

3 Congestion costs the urban traveler about \$750
4 in wasted fuel efficiency per year. If you believe that,
5 then there is a real argument for trying to improve our
6 system.

7 California's crumbling roads which, by the way,
8 Caltrans will acknowledge are near the bottom -- from the
9 standpoint of their condition, near the bottom of the
10 list in the United States, costs the average motorist
11 \$590 in vehicle maintenance per year that otherwise could
12 be reduced.

13 So -- I love this slide from the standpoint of
14 how dramatic it is. Once again, this is a third-party
15 analysis.

16 "Deficient roadway conditions contribute to more
17 than one-half U.S. fatalities. More than drunk driving,
18 more than speeding or failing to use seat belts."

19 So there is a need to improve our system that
20 goes beyond just the economics involved, that goes beyond
21 just the quality of life. It goes to the safety of the
22 traveling motorist. It costs the nation \$217 billion
23 which, by the way, is pretty close to what the U.S.
24 government spends federally on transportation construction
25 in this country.

1 Okay, so let's talk a little bit about what's
2 happening from a demographic standpoint. You all probably
3 all know this. I'm sorry to bore you with it. But
4 California's population is expected to grow 16 percent
5 over the next ten, 11 years. Vehicle miles traveled is
6 expected to grow 29 percent over that same period. And
7 California's vehicle miles traveled is growing ten times
8 faster than lane miles are being constructed.

9 I am not here to suggest that we need to build
10 roads all over this state; but I am here to suggest that
11 we need to improve the safety, improve the condition of
12 our current systems, and build some public transportation
13 that is appealing enough that people will actually use it.

14 So here's the fun part of this: If I were to
15 ask you -- and I've done this with lots of different
16 groups -- if I were to ask you what's it going to cost
17 you, as a driver, California -- the average California
18 driver to raise the gasoline tax 1 cent, and ask for a
19 quick answer without any consideration -- any thinking,
20 really, about it, and the typical answer that I've gotten
21 when I've asked this question, is \$100, \$200. 1¢ in the
22 average motorist's mind is worth \$100 or \$200.

23 So here's the arithmetic, here are the facts:
24 The average driver drives 12,400 miles a year in a car
25 that gets 22 and a half miles to the gallon and buys

1 554 gallons of gasoline per year. And every penny is
2 worth \$5.54 a year, or 46¢ a month.

3 10¢ is worth \$4.60 a month. It's about the
4 price of a six-pack of bottled water.

5 50¢ in gas is only \$23 a month, or about \$275
6 per year. And for \$275 a year, you could make an impact
7 on that \$750 in congestion costs and the \$590 a year in
8 maintenance costs on your automobile.

9 So it's really free if the agencies and the
10 engineers and the construction companies are efficient
11 and get the job done. And I'm here to tell you, as part
12 of that construction community, the agencies, the
13 engineering companies, and the construction companies of
14 this country can do a remarkable job of improving our
15 transportation system.

16 So the questions I have, maybe for you all and
17 for the Legislature and those that are really going to
18 weigh in on this matter, are what is a world-class
19 transportation system worth, how much would it save, how
20 much time would it save, how would it impact the quality
21 of life, which I think is very important. And the truth
22 is, what in the heck is the alternative?

23 We don't have an option but to deal with this
24 problem.

25 So these are my conclusions, these are the

1 conclusions that my company has reached, these are
2 conclusions that Transportation California has reached;
3 and I see the conclusion is somehow actually not in the
4 picture, so I guess I can maybe make one up here.

5 CHAIR PARSKY: Well, you fit right into this
6 Commission. That's okay. Don't worry.

7 COMMISSIONER EDLEY: We feel like we're in a
8 tunnel.

9 MR. DOREY: If \$16 billion -- if you believe
10 the Governor's Commission on Transportation in 2005,
11 unfunded needs were \$16 billion a year, 19 billion gallons
12 a year, including the diesel and trucks and so forth, is
13 84¢ per gallon is needed.

14 And it's not 84¢ a gallon ten years from now,
15 Fred, it's 84¢ a gallon today.

16 So I would encourage us to think about that,
17 to think about what we can do in this tax structure, what
18 we can do to put California in a competitive environment
19 from the standpoint of getting people around.

20 All user fees should be indexed to inflation
21 beginning immediately.

22 And here's the interesting one -- and the
23 Finance folks, I think, on the Commission will appreciate
24 this -- whatever we do, we don't need to wait for that
25 revenue to come in to begin the process. The state of

1 Florida is doing this regularly today, where they do
2 what's called gap financing. And they'll put a bid out
3 to do, say, a \$100 million project over two years, and
4 they will say to the prospective bidders, "We're going to
5 pay you over four," or, "We're going to pay you over
6 five."

7 So what the construction community then is
8 obligated to do, is get into the institutional investment
9 arena, arrange to have that financing gapped -- arrange
10 for gap financing, go build that job in two years, get
11 paid, and the institutional investor then will stand
12 ready to receive payment over five or six years, and the
13 financing is all considered.

14 So I think this is an important subject. And
15 I think the important thing maybe for you all to think
16 about as you contemplate this, is how does this fit into
17 what you're all dealing with? And I think this is it:
18 There is an opportunity here to take transportation
19 completely out of this debate. To take it out of the
20 budget debate, take it out of the funding debate, take it
21 out of what would be characterized as the tax structure
22 that you all are considering, and turn it completely into
23 a user fee for very little money.

24 \$23 a month per driver, 275 bucks a year would
25 raise 50¢, which would go a long way to really

1 affecting -- properly affecting the challenge that we
2 have.

3 So I would leave you with that. I appreciate --
4 really appreciate the opportunity to be here. And I hope
5 you'll consider these views as you contemplate this very
6 complex problem.

7 Thank you.

8 CHAIR PARSKY: Thank you.

9 Fred?

10 COMMISSIONER KEELEY: Thank you, Bill, very,
11 very much.

12 And, Mr. Chairman, if I could now introduce
13 John Boesel from CalSTEP. And he will provide a brief
14 testimony on this matter as well.

15 Thank you.

16 MR. BOESEL: Thank you, Fred.

17 Chairman Parsky and Members of the Commission,
18 my testimony is being circulated now.

19 I'm the president and CEO of CALSTART. We're a
20 not-for-profit corporation, headquartered in Pasadena,
21 with offices in the San Francisco Bay Area. Our goal in
22 life is to help improve air quality, cut greenhouse gas
23 emissions, reduce dependence on oil, and improve our
24 energy security, and create tremendous new economic
25 opportunities for people in the state by serving as a

1 catalyst and a strategic broker for the clean
2 transportation technology industry.

3 We work with an array of companies, representing
4 all the different technologies: Batteries, hybrid
5 systems, biofuels, natural gas, hydrogen fuel cells,
6 clean diesel, more efficient internal combustion engines.

7 We believe there are many paths to the future.
8 We definitely feel we are building a 21st century industry
9 and, therefore, are very appropriate for consideration by
10 your commission.

11 I was very honored to be part of a similar
12 blue-ribbon commission effort that we launched in 2005,
13 called the "California Secure Transportation Energy
14 Partnership," CalSTEP. And basically what we did was,
15 we were created to help develop a model plan, to make
16 California a state where our independence on the volatile
17 international market was reduced; and we are keeping more
18 of our energy dollars here in the state of California.

19 We were fortunate enough to have on that
20 Commission President Reagan's Secretary of State, George
21 Shultz, Stanford economist Jim Sweeney, executives from
22 DaimlerChrysler and Volvo Car Corporation; Andrew
23 Littlefair, the CEO of Clean Energy, Boone Pickens'
24 company; Neil Koehler, the CEO of Pacific Ethanol;
25 Dr. S.M. Shahed from Honeywell and 2002 SAE, Society of

1 Automotive Engineers, national president; Tim Carmichael,
2 a leading clean-air environmental advocate; then
3 Dr. Beverly Scott, who was the general manager of the
4 Sacramento Regional Transit District; a couple of
5 different clean tech investors; and Commissioner Fred
6 Keeley.

7 We actually had the luxury of spending that
8 18 months working in our blue-ribbon commission to
9 develop recommendations related to the transportation
10 sector. And we finally, in January of 2000, released
11 this report here. And we developed and proposed several
12 recommendations, many of which have been adopted.

13 One of them was very similar to the low-carbon
14 fuel standard which the Governor proposed. We had a
15 measure similar to Senator Steinberg's SB 375. We are
16 still working with the insurance commissioner on adopting
17 pay-as-you-drive insurance.

18 And then also, this then-Speaker Nunez adopted
19 our recommendation for providing funding for projects in
20 California. And he proposed AB 118, which the Governor
21 signed into law.

22 One of the key measures that we did propose,
23 that frankly has not yet been adopted, was something
24 called the "Energy Security Tax Realignment and Relief
25 Program." And that was basically, everybody on this

1 commission felt that if the price of oil started to drop
2 again, we would see less investment coming into this
3 industry and less activity, less progress toward our
4 goal.

5 So we felt that if the world oil price started
6 to drop, then a slow but steady increase in the gas tax
7 should be implemented in California.

8 We proposed a penny a month for ten years. So
9 basically, you get \$1.20 after ten years. And we felt
10 that this was something that industry could plan around --
11 plan for and take into consideration. And I think this
12 measure is very similar to the measure that has been put
13 forward by Fred Keeley today.

14 What's happened since we proposed this idea
15 is, a lot of other people have come on-board and really
16 supported similar concepts. And, in fact, right now, the
17 Alliance for Automobile Manufacturers, representing ten
18 different car companies, is recommending to Congress that
19 a floor on the price of gasoline be adopted, and that
20 floor be set at \$3.50 a gallon.

21 That's really a big-C change.

22 Thomas Friedman in the *New York Times* writes
23 almost weekly on this topic. He calls for a patriot tax.

24 When California's best-known venture capitalist
25 went to Congress and testified before Senator Boxer's

1 committee earlier this year, he also called for a floor
2 on the price of gasoline.

3 And another chairman of the Council of Economic
4 Advisors, under President Bush, one Mr. Mankiw, also has
5 endorsed the concept of taxing gasoline.

6 COMMISSIONER BOSKIN: That would be Bush II,
7 just to correct you.

8 MR. BOESEL: I'm sorry. Excuse me, Bush II.
9 Excuse me, sir.

10 And then so we just look at some of our member
11 companies, and we know that you take a company like ISE
12 in San Diego, that's trying to become a leader in
13 developing heavy-duty hybrid propulsion systems. If
14 they can estimate that the price of gasoline will be at
15 a certain price, they know that their payback on their
16 product will be better than if the price were low.
17 Therefore, they're going to have more success selling
18 that product in the marketplace.

19 California has a number of very exciting
20 next-generation biofuel companies. Their business plan
21 always improves when they can cite and have some evidence
22 for a higher price of gasoline. And when that business
23 plan improves, they attract more investment. So I think
24 this policy will help drive this industry forward in
25 California.

1 Lastly, I just want to say that the Governor's
2 Executive Order, beyond AB 32, which was the 15 percent
3 below 1990 levels by 2020, the Governor's Executive Order
4 calls for an 80 percent reduction below 1990 levels by
5 2050. That's enormous. It bucks all trends over the
6 last decades of population growth and carbon output.

7 So if we're really going to change things, we
8 certainly need the regulations, like the Pavley bill,
9 the low-carbons fuel standard. But having that pricing at
10 the pump is critical.

11 Thank you very much.

12 CHAIR PARSKY: Thank you very much.

13 Fred --

14 COMMISSIONER KEELEY: Mr. Chairman, I'd be glad
15 to conclude.

16 CHAIR PARSKY: No, no, I wanted to make sure
17 that in your conclusion, you summarized the nature of
18 the tax that's being suggested and the direction for the
19 revenues.

20 COMMISSIONER KEELEY: Thank you, sir.

21 Mr. Dorey and Mr. Boesel, thank you both very,
22 very much for spending a day with us.

23 Mr. Chairman, on page 1 of the document that
24 the working group prepared for the Commission, it goes
25 through each one of the objectives that the Governor

1 outlined for us in terms of what our task is here relative
2 to the entire tax package that we'll be considering.

3 I do believe that, with a very straight face and
4 based on the kind of testimony that you've heard today,
5 that each and every one of the Governor's objectives for
6 us is met through this particular proposal.

7 And, Mr. Chairman, I will summarize exactly
8 what that is. You would take the existing excise tax on
9 gasoline in California, which is 18¢ a gallon, add another
10 18¢ a gallon. Then every year thereafter, for ten years,
11 you would take that 18¢, increase it by the California
12 Consumer Price Index, and 7¢. You would do both of those
13 things. So that where you would end up is essentially
14 where Mr. Dorey would like us to end up tomorrow, it will
15 take us ten years to get there, but we would get there.

16 The expenditures are all governed by Article XIX
17 of the Constitution. And in the draft legislation that
18 you have in front of you, it would use the first
19 half billion to offset general fund obligations to retire
20 transit and transportation bonds.

21 The next, roughly, half billion would be used
22 for those activities, consistent with Article XIX, that
23 are also contained in AB 32 and SB 375, which are those
24 sort of new and creative approaches to reducing greenhouse
25 gas emissions, but they have to be done in compliance

1 with Article XIX, so they have to be done in terms of
2 streets and roads and highways.

3 Then you would take essentially the remaining
4 funds, which is the vast bulk of the money that this would
5 raise, and you would split it evenly between Caltrans and
6 local governments for maintenance, repair, and improvement
7 of the state highway system and the local government
8 system.

9 What it would also do, is that it contained --
10 the bill that we have submitted to you also contains a
11 provision that asks the Legislature to develop a mechanism
12 which would allow for a refund to low-income individuals
13 to reduce the regressivity of this tax.

14 We had wrestled with this and ultimately
15 concluded that we could not do that in this bill because
16 of the restrictions contained in Article XIX of the
17 Constitution.

18 We had Legislative Counsel in all of our
19 meetings, and Legislative Counsel wrote the bill that we
20 have here so that it is, in fact, in compliance with
21 Article XIX of the Constitution, as well as all other
22 provisions of the Constitution. That was the one issue
23 that we have to punt on to the Legislature, is how to
24 effectuate a rebate. But the provision for that is in
25 the statute.

1 Mr. Chairman, I really appreciate your
2 indulgence in allowing me and Mr. Dorey and Mr. Boesel
3 to make a lengthy presentation on this. I want to thank
4 all of the folks who were involved in the working group
5 on this, and your kindness in posting this on the
6 Commission's Web site when it was available. I appreciate
7 it.

8 Thank you, Mr. Chairman.

9 CHAIR PARSKY: Thank you very much.

10 And I also want to pay special thanks to all
11 the people that worked hard on this proposal. It was a
12 gargantuan effort.

13 I think what I'd like to do, if it's all right,
14 is to ask Michael Boskin to comment or describe another
15 proposal that is on the table. Then we'll come back. I
16 want to make a few comments about the dispute resolution
17 form that is part of the package.

18 But I'd like to then ask for comments or
19 questions about each of these.

20 But, Michael, why don't you go ahead and --

21 COMMISSIONER PRINGLE: Excuse me, Mr. Chairman,
22 about each of what? Of this pool of things?

23 CHAIR PARSKY: Yes, this pool of things.

24 We've had an opportunity on the first part, but
25 I think --

1 COMMISSIONER PRINGLE: All right, I can wait on
2 this because I do have some comments.

3 CHAIR PARSKY: Right. You'll have that
4 opportunity.

5 COMMISSIONER KEELEY: Thank you very much.

6 MR. DOREY: We're done?

7 CHAIR PARSKY: Yes. You're welcome to stay.
8 In fact, if you really want to help the Commission on the
9 rest of our activities that we're doing, we'd welcome it.
10 It's perfectly okay. But we really thank you very much.

11 MR. DOREY: I appreciate it. If there's
12 anything more that we can add to this discussion, we'd
13 be happy to do it.

14 Thank you all very much.

15 CHAIR PARSKY: Thank you.

16 Michael?

17 COMMISSIONER BOSKIN: Yes, I had two things.
18 Let me go over them very, very quickly.

19 The first one, the minimum tax. One of the
20 very disturbing things about the proposal is the removal
21 of millions of people, millions of Californians, from
22 paying any contribution to the state general fund and,
23 therefore, contributing to, even in a trivial way, a tiny
24 way, the financing of the collective commonwealth public
25 services.

1 I personally prefer a 1 percent minimum tax.
2 And Becky has mentioned \$100, or \$50, which would be
3 \$2 a week, or \$100.

4 I think it is the single biggest mistake that
5 has been made in tax policy, has been to remove large
6 numbers of people from any responsibility for financing
7 government. While certainly ability to pay needs to be
8 one of the criteria, benefits principle is another.
9 Virtually all such individuals and families benefit
10 from roads, from our security, from our schools. And I
11 could go on and on and on. But the fact of the matter
12 is, it is very troubling, and it is dangerous, literally
13 dangerous in a democracy to create a situation where we
14 are going to be heading towards 50 percent of the
15 population paying no taxes.

16 They'll be paying local sales taxes, I agree
17 with that, but they won't be paying state sales taxes or
18 state income taxes into the general fund. And
19 California's already apparently first in the fraction.
20 It excludes from its income tax, among the 41 states that
21 have an income tax, according to the Tax Foundation. And
22 I think this is a very explosive thing, politically, and
23 dangerous and unwise. It's basically making half --
24 between 40 and 50 percent of the population kind of
25 totally severing any tie between taxes and spending for

1 them, and I think that's a very bad idea. So that's one
2 proposal.

3 The second one I will speak to very briefly.
4 I did not bring the CEO of Chevron here. But it seems
5 to me to be perhaps the single-most foolish thing the
6 State does, to have this ban on offshore oil. It is
7 quite sensible to be extremely concerned about the
8 environment. So any exploration and drilling offshore
9 should be done under extremely strict environmental
10 standards. But compared to 1969, when the Santa Barbara
11 spill unfortunately happened, the energy industry has
12 moved on. All of the State's resources could be accessed
13 from onshore, because you can now go seven miles from
14 onshore to offshore; and California only has full rights
15 over the first three miles.

16 All the acreage beyond that, which is federally
17 owned, in every other part -- and the other oil-producing
18 areas, like especially the gulf, the federal government
19 shares the revenues three-eighths with the states.

20 Now, some portion of that goes to the local
21 counties, the counties along the border, like it would be
22 Santa Barbara and L.A. and so on -- and Santa Cruz, if
23 there's any oil off there that Fred would like to get
24 some of the money on to pay for roads.

25 But the single-most glaring thing about all of

1 this to me is, that's never going to be accessed. So
2 you think about the worst thing you can think of, someone
3 sadly dies, the money in their checking account, they
4 can't find any relatives. At least that money goes to
5 the state.

6 In this case, it's just going to lay there
7 forever. This is the only source of revenue that not a
8 single taxpayer would complain about. They want the right
9 to be able to do it, and they're willing to share the
10 revenue with the State. It is about the only tax we
11 could think of -- royalty tax, whatever you want to call
12 it -- the revenues the State would get from this, are the
13 only revenues that cause no economic distortions, because
14 that oil isn't going anywhere else -- or natural gas, or
15 whatever it is.

16 So the proposal is -- and because it depends
17 the price of oil, worth \$71 in the worst recession in a
18 quarter century, God knows if it's going to go back up
19 to \$140; but over a span of time, it's likely to be
20 considerably higher than it is right now. In some
21 years, it will collapse and others it will be higher,
22 et cetera.

23 It seems to me, it would be the height of folly
24 that the State doesn't even explore what it could get out
25 of all this. So the proposal is to suggest the Governor

1 and the Legislature allow offshore drilling under the
2 best feasible commercial terms for the state under
3 extremely careful environmental safeguards. This would
4 generate from a few billion dollars to many tens of
5 billions of dollars, depending on all of that. But it
6 seems to me to be, number one, the height of arrogance
7 to suggest that the State shouldn't even consider the
8 opportunity cost of leaving it there forever.

9 And with all the needs we have to just say that
10 we're going to not even think about the possibility under
11 strict environmental regulation, accessing what such other
12 environmental Neanderthals as the British, the Norwegians,
13 and the Dutch, who go after every molecule they can
14 possibly find, that we somehow are going to rule that
15 out, it seems to me, to be about the single-most foolish,
16 backing it up from a commonsense policy perspective
17 despite -- I mean, I understand it draws great emotions
18 and it mobilizes environmental lobbies and energy lobbies
19 and all that sort of stuff. It just seems to me to be
20 the height of folly for us not to consider the State ever
21 getting the benefit of that revenue.

22 And if what Fred and these gentlemen would like
23 to see in our environmental future, getting away from oil,
24 it means it will stay forever and eventually we'll have
25 something else. I think that's 50 or 100 years off, not

1 five. But, in any event, leaving it there and never
2 getting any of the revenue, it seems to me would be a
3 great, great sin to the state.

4 CHAIR PARSKY: Okay, let's just pause here and
5 ask questions.

6 COMMISSIONER BOSKIN: And by the way, I should
7 say because of the uncertain revenue, I suggest that the
8 revenues go into the rainy-day fund, and they come out
9 that way. So they can find one-time expenditures, they
10 can add to the reserve, they can lessen the need for
11 other taxes to be diverted there, et cetera, et cetera,
12 et cetera. But it's not totally predictable, so it's
13 just an additional source of revenue. So in that sense,
14 that's important to mention.

15 CHAIR PARSKY: Okay, Chris, and then I'll ask
16 Curt to come back because I know he's got some comments
17 or questions.

18 Chris?

19 COMMISSIONER EDLEY: Yes, with respect to
20 Michael's -- I mean, I will say that I followed everything
21 you said except your sort of suggestion that there is
22 something wrong with folly, because this being --

23 CHAIR PARSKY: Because we are engaged in it, is
24 that why?

25 COMMISSIONER EDLEY: Now, you tell me.

1 COMMISSIONER BOSKIN: It undermines a lot of
2 Shakespeare's plays.

3 COMMISSIONER EDLEY: It does.

4 I guess what I really don't understand is the
5 analysis with respect to the sort of the skin in the
6 game, small D, democratic point regarding paying taxes.
7 Specifically, paying income taxes, in the sense that if
8 the issue really is, small D, democratic engagement, do
9 you feel like you have a stake in the decisions that are
10 being made, do you feel like you have a stake, even in
11 the structure of the tax system?

12 Then I'd say that, on the one hand, people
13 certainly have a stake in whether or not there are
14 revenues to produce the services upon which they depend.
15 But even putting that to one side, wouldn't the logic of
16 your position be satisfied if everybody filed a return,
17 but then people for some ways up the income distribution
18 got a refundable credit, as opposed to having a positive
19 tax obligation? They'd certainly still have a stake in
20 what tax policies are. So that's one question.

21 And then I was going to go to the oil-tax issue.
22 But if you want to --

23 COMMISSIONER BOSKIN: Yes, there are two
24 separate things here. I think Richard and others have
25 rightly said, they're issues of the salience, what people

1 have in their mind about whether they're paying something,
2 if it's withholding, or whether they're paying something
3 when they go buy a pair of jeans, et cetera and so on.
4 So one point is, this participation, in that sense.

5 The other thing is, if we actually reduce the
6 price of expanding government spending to zero, people
7 will demand more government without limit because they
8 pay nothing. And even though it's tiny, it's important
9 for people to understand that if the government grows,
10 it may be worth it, that there will be some small
11 consequence for them. So that's my point.

12 COMMISSIONER EDLEY: But my proposal satisfies
13 that; right? Because if I'm getting, let's say, a \$250
14 refundable credit but I support the expansion of
15 government, I would have -- I would logically be concerned
16 that my \$250 refundable credit is going to disappear. So
17 I have a stake in what decisions are being made. Don't
18 spend more money on prisons, save my \$250 refundable
19 credit.

20 And let me -- I'm not making an academic point
21 here, because I'm also interested in whether or not we
22 can tweak the progressivity of our PIT strategy,
23 especially kind of in the zero to \$80,000 range. If we
24 can tweak that by taking revenues, such as the revenues
25 that might come from a severance tax or royalty on new

1 drilling, and putting that into a refundable credit.

2 And so I don't find your argument that people
3 need to have skin in the game all that compelling; but
4 what I'm wondering is, just on your logic, would people
5 still --

6 COMMISSIONER BOSKIN: The logic is the total
7 size of spending. They should have a stake in the total
8 size of spending.

9 Everybody has a stake in trying to get as much
10 as they can of whatever the size of the pie is going to
11 them, as refundable credits or as subsidies for
12 alternative energy or for subsidies, as Richard probably
13 points out, for some of these breaks that are probably
14 unnecessary in the corporate tax. Everybody's going to
15 try to maximize that.

16 But for any given level, you should have a stake
17 that if it goes up, you pay something. That's kind of a
18 basic minimal proposition. It won't be very much in this
19 situation. It will be a couple of bucks or 4 bucks a week
20 or something like that. But, in any event, it's something
21 rather than nothing.

22 COMMISSIONER EDLEY: Well, I guess I'd just
23 have to say not proven. Because it still seems to me
24 that even people who are positively paying taxes still
25 could be in favor of more government spending if they

1 think that they will be beneficiaries of it.

2 COMMISSIONER BOSKIN: There's no doubt. I'm
3 not disagreeing with that at all. I'm just saying, if
4 the price to them is zero, they have no incentive
5 whatsoever to even care about a cost-benefit analysis
6 because the cost to them is zero. There's just no
7 positive cost whatsoever to them.

8 COMMISSIONER KEELEY: Mr. Chairman, if I may,
9 just make one comment?

10 Mr. Boskin, to follow up on Chris' point, I
11 think what's happened as part of your argument, is that
12 you've isolated the personal income tax, and said that
13 folks don't pay that, and therefore -- and then you've
14 gone on to talk about whether they have a stake in their
15 government, and how much it spends and what it does, and
16 so on.

17 But, quite frankly, low-income folks pay sales
18 tax, they pay gas tax, they pay excise taxes -- they pay
19 all kinds of taxes. And the fact that they don't pay an
20 income tax or they have --

21 COMMISSIONER BOSKIN: You don't get correctly
22 what I said, Fred. I'm sorry.

23 COMMISSIONER KEELEY: Oh, I'm sorry.

24 COMMISSIONER BOSKIN: I made very clear that
25 we're removing many millions of people from paying the

1 State's general fund sales tax, on top of not paying the
2 income tax. That's the problem.

3 COMMISSIONER KEELEY: Well, if I understand
4 the BNRT proposal correctly, everything that is
5 currently taxed under the sales tax will continue to be
6 taxed under the BNRT, and a whole range of activities
7 and transactions --

8 COMMISSIONER BOSKIN: There is a great --

9 COMMISSIONER KEELEY: If I might finish -- if
10 I might finish -- a whole range of activities that are
11 currently not taxed, will be taxed under the BNRT.

12 But I'm trying to go to the -- if I understood
13 the intellectual impact of your argument, it's that
14 people need to pay taxes in order to have an appreciation
15 for what those taxes purchase and what their government
16 is doing with it. And I simply wanted to make the point
17 that I think poor people, low-income people, pay taxes
18 and probably pay a larger portion of their income in
19 various and sundry taxes than others already, irrespective
20 of what happens on the PIT or what we do with the BNRT or
21 the sales tax.

22 COMMISSIONER BOSKIN: I don't see your
23 arithmetic. But leaving that aside --

24 COMMISSIONER KEELEY: Okay.

25 COMMISSIONER BOSKIN: Leaving that aside, I

1 think there are big issues about who will wind up paying
2 the BNRT. And it certainly will be hidden.

3 No one is talking about somebody walking in and
4 getting a sales tax added on top of something. It will
5 be embedded in the price. So we're basically removing
6 millions and millions of people from having any direct
7 contact with the general fund and anything they do that
8 pays for the general financing of state services, even on
9 a trivial basis. That is a big worry for me, and I think
10 it's going to be a big worry for a lot of other people.

11 COMMISSIONER DE LA ROSA: Can I say something?

12 CHAIR PARSKY: Okay, but, Chris --

13 COMMISSIONER EDLEY: That's all right if we're
14 on this subject.

15 CHAIR PARSKY: Okay, go ahead, Edward.

16 COMMISSIONER DE LA ROSA: Well, I'm sympathetic
17 to the argument. But I think that I would argue that
18 there are many people in the state of California that
19 don't really understand what kind of benefit they're
20 getting from the personal income taxes that they pay
21 today, and that includes rich people.

22 COMMISSIONER BOSKIN: No, I would include a lot
23 of rich people in that, too, by the way.

24 COMMISSIONER DE LA ROSA: I'm very serious about
25 this. And I think that, it seems to me that there's

1 another angle to that issue, and that has to get to the
2 notion of citizenship. You know, and I don't know that
3 that adjustment helps promote citizenship. You know, I
4 just think -- I think that many of the people that we're
5 talking about are just trying to get by. And I don't
6 think they feel like they have any control over what the
7 Legislature does with their tax dollars. In fact, I
8 don't think that they think very much about where their
9 tax dollars go.

10 And so that causes me to question -- and I
11 appreciate the fact that you offered that explanation,
12 because I've thought a lot about this, about this linkage
13 between the tax dollars that you pay and the services or
14 the infrastructure that you get back. But I'm a little
15 bit skeptical that taxing the lower-income quintiles, I
16 guess, of some representative amount causes them to feel
17 as though they have a stake in the government that they
18 didn't have before, and that it adds to their notion of
19 citizenship. I think they'll feel resentful about that
20 tax, like they feel resentful about the taxes that they
21 have to pay today. And that's my opinion.

22 CHAIR PARSKY: Chris, you had some questions for
23 Fred?

24 COMMISSIONER EDLEY: I guess for both of them.
25 Fred, how do you deal with the revenue-neutrality issue

1 for a package as a whole? Or is there a way to deal with
2 the --

3 COMMISSIONER KEELEY: Well, if I understand how
4 it works it -- and Mr. Genest, I need a little help on
5 this -- make up an answer that will make me happy, would
6 you, please?

7 CHAIR PARSKY: Go to it, Michael.

8 COMMISSIONER KEELEY: Mr. Genest, I don't know
9 how you score funds that are restricted. So, for example,
10 the excise tax on gasoline, which is restricted by
11 Article XIX, I don't know if you call that "general fund
12 revenue," and I also don't know whether we are scoring
13 this package as revenue-neutral relative to the general
14 fund or how we're treating special funds. I just don't
15 know how we're doing that.

16 MR. GENEST: Well, unfortunately, that is a
17 tax, so the proceeds of a tax, if you raise the tax, it's
18 not revenue-neutral. And in the sense of the Legislative
19 Counsel scoring it, they'll call that a super-majority
20 bill even though it's a tax increase, even though it's
21 dedicated.

22 It would, however, it sounds to me -- and you
23 can check with Mr. Parsky -- but I think it fits into
24 Category 3. I don't know that Category 3 is necessarily
25 restricted to revenue-neutral. I'm not sure of that.

1 But it can't be scored revenue-neutrally. I don't see how
2 you could.

3 CHAIR PARSKY: Let's put aside for the moment
4 where it fits, but -- John?

5 COMMISSIONER COGAN: Fred and Curt, part of your
6 proposal, Fred was to replace some of the lost sales tax
7 revenue on gasoline, Prop. 42 revenue, and so there's not
8 an issue there of revenue neutrality, I don't think. And
9 so I'm sympathetic to the idea.

10 One concern I have is, are there other earmarks
11 of retail sales or any other tax that we're proposing to
12 modify that would be affected by the elimination of the
13 retail sales tax or the corporate tax? Is there any other
14 that you can think of?

15 I just don't want to have a lot of people,
16 claimants coming in, saying -- demanding equal treatment
17 if we were to go down this road.

18 MR. IBELE: I was going to say no, but Mike just
19 mentioned the spillover impact on the sales tax.

20 COMMISSIONER COGAN: Do you want to elaborate
21 on it a little bit?

22 CHAIR PARSKY: Briefly, Michael.

23 MR. GENEST: It's hard to be brief.

24 It's money that ends up to the benefit of the
25 general fund through a circuitous route, and it starts out

1 as sales tax on gasoline, and it gets spilled over into
2 this strange formula -- it's not worth going over how, I
3 don't think. So there is an impact on the general fund.

4 If you eliminate -- if you just eliminate the
5 sales tax on gasoline all together, which is -- I guess
6 I was mistaken, I thought that was not what you were
7 proposing. But if that's what you're proposing, then you
8 have to have some other revenue to replace that.

9 And I think, Mark, you've made that calculation
10 already or --

11 MR. IBELE: Well, no. And we've included the
12 whole 5¢, 5 percent in our calculations.

13 CHAIR PARSKY: So presumably, when everything
14 was fully phased in, it would make up for it, but not have
15 designated where to go. But it would make up for the loss
16 in the sales tax, or revenue related to the sales tax on
17 gasoline.

18 MR. IBELE: Right, right.

19 MR. GENEST: So the spillover thing, no one can
20 predict it -- because of the way the formula works, no one
21 can predict whether it will exist as a revenue five years
22 from now.

23 COMMISSIONER PRINGLE: So, Mr. Chairman, that
24 is not an issue. It just is -- once Prop. 42 was passed,
25 according to Mr. Genest's earlier discussion, there was

1 this opportunity where money went into the general fund,
2 and then flowed into the general fund for other transit
3 uses or other transportation functions or such. But the
4 point of the matter is, it's never been something
5 calculated until the last couple of years, but it's still
6 tied directly to the sales tax on gasoline.

7 So I think your question, John, was, are there
8 other types of dedicated portions of the sales tax. And
9 I think Prop. 42 is the only area where there is a
10 dedication of a --

11 COMMISSIONER COGAN: General --

12 COMMISSIONER PRINGLE: -- general fund use,
13 even though we have dedicated sales taxes, but we're not
14 proposing to eliminate them.

15 You know, this piece goes here or this piece
16 goes there. The 1 percent of personal income tax for
17 mental-health programs and things like that, we're not
18 looking to challenge any of those. So those are
19 dedicated. But they have not been included in the list
20 of reductions.

21 CHAIR PARSKY: This has but that didn't.

22 COMMISSIONER KEELEY: Mr. Chairman, you did ask
23 me a question about the revenue-neutrality question.

24 Let me say a couple of things about that, and
25 I hope that, to quote Gerry Parsky, all I'm asking you

1 to do is just think about this. Just think about this.

2 CHAIR PARSKY: Does that go with the cowboy
3 outfit?

4 COMMISSIONER KEELEY: Just think about this.

5 Revenue neutrality -- I'd like to make two
6 points on it. Number one -- and I'm sorry to be such a
7 broken record on this -- but that is a concept that the
8 Governor has spoken about but is not in the Executive
9 Order. And so I don't believe that we are bound by that.

10 I especially don't think we're bound by it, now
11 that -- when you and Commissioner Cogan and Commissioner
12 Edley made your visits to Sacramento last week, and over
13 the weekend when I talked to the President Pro Tem of the
14 Senate, and it was disclosed that the leadership and the
15 Governor are no longer imagining that there will be a
16 package sent to them that they will then -- in bill form,
17 that they will then put upon the floor of the Assembly
18 and the Senate and ask for an up-or-down vote.

19 If we were still bound by that, then I think
20 the revenue-neutrality issue is much stronger. But the
21 fact that it's neither in the Executive Order, nor does
22 the strategy for implementation any longer involve an
23 up-or-down vote, I think what we should do is submit the
24 package we think is the best package for California.

25 Now, I'll make this argument again on Monday,

1 but I strongly encourage the Commission, when we put this
2 package together -- and this is the phrase that I learned
3 in the Legislature -- and, Commissioner Edley, there are
4 some good things to learn in the Legislature.

5 COMMISSIONER EDLEY: Yes.

6 COMMISSIONER KEELEY: Listen to your
7 enthusiasm -- but here's one. Here is one.

8 COMMISSIONER EDLEY: Name a half.

9 COMMISSIONER KEELEY: I'll name one, and that
10 is, I think the people -- and I would certainly include
11 Senator Morgan and Speaker Pringle in this, when they
12 were in the Legislature, that you should always be working
13 towards a principled compromise, and you should never ask
14 the other person to compromise their principles.

15 And I think the best work -- and you may say
16 that the Legislature doesn't do much good work, but when
17 it does, it's good work and its best work. It's when
18 they follow that, I believe. And I think that that's
19 what the Chair has asked us to all do for the last eight
20 months, is to see where we can reach a principled
21 compromise without compromising our principles.

22 And I will revisit this topic and ask the
23 commissioners when we are stretching to find that
24 principled compromise, that this is one of the pieces
25 that goes in Recommendation Section 1.

1 And rather than taking you through all those
2 arguments today, I would simply like to put a placeholder
3 in to be able to do that at some point on Monday.

4 Thank you, Mr. Chairman.

5 COMMISSIONER EDLEY: May I try to make a
6 constructive suggestion here?

7 Fred, I would hope that you and Curt would
8 consider that if there were a way to disaggregate your
9 proposal so that there's a piece of it that is intended
10 to merely ensure that we don't vitiate the purpose of
11 Prop. 42 -- 19, 40 -- 76?

12 COMMISSIONER KEELEY: 42.

13 COMMISSIONER EDLEY: Yes, thank you. That we
14 don't vitiate the purpose of Prop. 42. In other words,
15 that we preserve the current flow dedicated to
16 transportation, and have revenue neutrality in that sense,
17 I would strongly support including that within Category 1.

18 The aspiration that goes beyond that, to provide
19 the additional revenues, I think the policy case for it
20 is very strong. But, frankly, I think the two-thirds
21 requirement makes it, from my point of view, not
22 acceptable as part of the core package because I really
23 would prefer, notwithstanding Richard's injunction that
24 we try to hold off political considerations as much as
25 possible, I really would prefer that we present the

1 Legislature with something that moves us towards the
2 future but that can be adopted by majority vote rather
3 than two-thirds vote.

4 COMMISSIONER KEELEY: I would be glad to do
5 that. Mr. Chairman, I'd be glad to work on that over the
6 next few days.

7 Let me make two comments on that.

8 Number one, the Prop. 42 sales-tax problem that
9 is now identified, is a problem that occurred because
10 there is a proposal to eliminate the state sales tax.
11 Not that I made a proposal -- okay. So I know, in part,
12 what's being asked, is that I solve a problem that got
13 created elsewhere in this, but I'm perfectly willing to
14 work on that. It's not a new concept to me.

15 But secondly, I think there are many ways to
16 address that. For example, we could say, let's take a
17 corresponding -- this is what occurs to me now -- don't
18 eliminate the bank and corp. tax. There's \$9 billion.
19 Don't eliminate that.

20 And, you know, my proposal is three and a half
21 billion dollars in the first year. So, I mean, I'm
22 willing to examine the package and look at it so that we
23 can find a way to get to revenue neutrality.

24 I would not like to take all of the work done
25 on this particular aspect of our proposal and say that it

1 is the thing that is causing the imbalance in revenue
2 neutrality. Everything is related to everything else in
3 this proposal.

4 So maybe what I can do is in Year 1, 2, 3, 4,
5 and 5, show you a way to get three and a half billion in
6 the first year, 3.75, et cetera, et cetera, without
7 vitiating the proposal I've made, while still protecting
8 Prop. 42, which is an issue over in the sales tax.

9 And I suspect where I'm going to go with that
10 is to try to look at the bank and corp. tax. But I will
11 be glad to do it. I'll take it in earnest effort at it.
12 I'll do my best. I'll meet with these folks about it.

13 COMMISSIONER BOSKIN: You should save your time,
14 Fred. I think what's going to happen, and it's very
15 clear, if we're going to deal with it, there will be some
16 carve-out to deal with it. Your proposal should rise or
17 stand on its own. I don't think you should be burdened
18 with how they do all this other manufacturing.

19 COMMISSIONER PRINGLE: Mr. Chairman, if I could.

20 CHAIR PARSKY: Curt, do you have a comment?

21 COMMISSIONER PRINGLE: First off, what I would
22 propose is that the proposal gets voted on separately.
23 And if it needs to be added into some other portion of
24 our report, I personally don't think it should be a part
25 of Track 1.

1 What I am going to suggest maybe shouldn't be a
2 part of Track 1, either, maybe it should be a part of
3 Track 3, and just making sure that when the Legislature
4 sees our package, they realize that we are aware of this
5 interplay with transportation funds.

6 And all I would suggest, Chris, is to support
7 a per-gallon gas and diesel tax and excise tax that would
8 increase within the phase-in period to equate directly
9 year by year through that phase-in period with the
10 reduction in sales tax. So all we are doing is creating
11 a gas tax, which on this side is protected under
12 Article XIX of the Constitution, that says it can be used
13 only for transportation purposes, anyway.

14 And as we reduce the sales tax, we increase
15 the gas tax proportionately, so that the one protection
16 that's in place on Prop. 42, which is constitutional
17 based on the sales tax, is that sales tax goes down, you
18 increase the gas tax and you are falling under another
19 constitutional protection under Article XIX.

20 You could do it directly revenue-neutral within
21 the phase-in period of our proposal.

22 You know, I don't necessarily ask that that be
23 a part of our Number 1, Track 1. Just make sure that the
24 Legislature knows that we are concerned about that, and
25 it should be a part of Track 2.

1 COMMISSIONER EDLEY: That's sort of what I had
2 in mind. And I at least -- personally, I would support
3 that in Track 1.

4 COMMISSIONER POMP: Mr. Chair, I have a quick
5 question for the good doctor.

6 Michael, what you were describing is what you
7 would call a tax on economic rents; is that right? The
8 royalty is essentially an economic rent?

9 COMMISSIONER BOSKIN: There are a variety of
10 ways to think about it, yes. But these are on state and
11 federal lands; they're not on private property.

12 COMMISSIONER POMP: Right.

13 And would you say a severance tax is a tax on
14 economic rents as well?

15 COMMISSIONER BOSKIN: It depends on how it's
16 imposed and where it's imposed, but it could be.

17 COMMISSIONER POMP: It could be?

18 COMMISSIONER BARRALES: I have a question.

19 CHAIR PARSKY: Ruben?

20 COMMISSIONER BARRALES: I just want to clarify.
21 When we talk about net neutrality, the elimination of
22 the state general fund portion of the sales tax, just to
23 be clear, the Prop. 42 dollars net that is still in our
24 proposal; in other words, it's not identified, but it
25 still is as it phases in?

1 CHAIR PARSKY: Yes, right.

2 COMMISSIONER BARRALES: So it wouldn't require
3 any additional tax above and beyond the proposal that was
4 made this morning but, rather, potentially, if it's
5 important, a designation of some other fund?

6 CHAIR PARSKY: Right, right.

7 COMMISSIONER BOSKIN: Well, if it was done in
8 the way Curt suggested, if his numbers were correct, an
9 8¢ increase in the excise tax in Year 5 to compensate
10 for the reduction in the sales tax, et cetera, that would
11 mean that you would need less money in the general fund
12 because the money wasn't being diverted. It had the gas
13 tax. So you could have a slightly lower BNRT, or you
14 can use the revenue for something else.

15 CHAIR PARSKY: That's the relevant relationship.

16 COMMISSIONER BOSKIN: You could do more on the
17 income tax, you could do other things, right.

18 COMMISSIONER PRINGLE: Mr. Chairman, one
19 additional thing. And there's a lot of talk about what
20 is a two-thirds vote and what is not. I just would like
21 to suggest -- I believe it's all a two-thirds vote. And
22 I don't believe that is an insurmountable task to get
23 two-thirds vote at the Legislature if we proceed, as you
24 suggest, Mr. Chairman, and try to build a strong consensus
25 among this group.

1 I don't know if the Legislature will put in as
2 much work, or individual members of the Legislature will.
3 Certainly some members will, as we all have. But I
4 believe if they see the interplay and the value with the
5 construction of it, a two-thirds vote is something I
6 think one protects us.

7 So we shouldn't just argue that everything we
8 do should be a majority vote because, in fact, if you pull
9 out any single piece -- for example, an excise tax can't
10 be written in the same bill, I don't believe, as many of
11 the other taxes that are. The BNRT may not necessarily
12 be in the same bill. So it's kind of a bill-by-bill
13 distribution. And if one bill increases any more, then,
14 in fact, it could be a two-thirds vote. So you have got
15 to be very careful as to -- you can't tie seven bills
16 together and say that, "That is a package; therefore,
17 they're all tax neutral together." It is a bill-by-bill
18 inquiry as to the tax neutrality of that. And there have
19 been many challenges on the whole concept of what is
20 two-thirds and what is majority.

21 I think we all talk about, we want it all tax
22 neutral for a lot of reasons, but I also think it would
23 protect our package -- our overall package to be complete
24 if we don't just assume that it's going to be a majority
25 vote product.

1 COMMISSIONER POMP: What is the window for
2 neutrality? I mean, let's say that there is this majority
3 vote. Neutral over what period?

4 CHAIR PARSKY: Well, there has to be an
5 assessment made by the Legislative Analyst's Office over
6 the first year of implementation, and then over either a
7 three-year or five-year assessment of neutrality.

8 I would just step back a minute and ask the
9 Commission to focus on the interplay of the package as a
10 whole.

11 What I think is very important is that we
12 continue to look at this package together.

13 The staff has been attempting to assess that
14 package in a way that is revenue-neutral. And I think
15 it's very important that the message not go to the
16 Governor and the Legislature that this Commission is
17 saying "Pick and choose," but, rather, "Look at the
18 package as a whole." And that's what I'd ask us to stay
19 focused on.

20 Let me just suggest one other thing, and then
21 I'm going to come back and ask everyone to think about.
22 Think about.

23 For those of you that thought that we were going
24 to just vote today, I hope that I don't disillusion you
25 given the exchange that's gone on.

1 I just want to make one other comment. A
2 proposal that is in your package that you can look at, if
3 you haven't already, would be the establishment of a tax
4 appeals tribunal or a dispute resolution forum. The
5 proposal simply would say that California should create
6 an independent body with tax expertise to resolve disputes
7 between the State and taxpayer. A taxpayer should be able
8 to appeal for a ruling from the independent tribunal prior
9 to having to pay the tax bill in question.

10 Relatively simply, with a lot of explanation.

11 Throughout the Commission process, whenever this
12 was raised, it received a significant amount of support.
13 And so I would think that the Commission would want to
14 continue to keep that on the table as a possible part of
15 Section 1, which the State could enact. And there is a
16 rationale and a background piece in the materials about
17 it that I want you all to think about.

18 What I would suggest -- and we have still
19 remaining the public comment period, which I intend to
20 stay for; however, I know a number of commissioners we
21 have extended beyond their time frame. But I would
22 suggest the following for the Commission to think about
23 between now and Monday, or between now and September 20th,
24 which is the final day at which this Commission expires
25 or our report is due. My suggestion would be that the

1 Commission think about the package of changes that was
2 first described -- first described by Chris and John as a
3 package of changes that we could support, hopefully
4 unanimously, that we could support, with the caveat that
5 was really contained -- with a couple of further analyses
6 that need to go on, that need to be aired clearly.

7 COMMISSIONER EDLEY: And let's be clear about
8 what exactly those are.

9 CHAIR PARSKY: One, it seems to me, that we need
10 to attempt, with all the caveats that are embodied in it,
11 attempt to have the staff suggest to us and discuss the
12 overall distribution or incidence impact of the package
13 as a whole.

14 We've seen, at least from the staff, supported
15 by a number of us, the impact of the changes in the
16 personal income tax alone. And we may have disagreements.
17 But I think many of the commissioners have indicated that
18 that retains the progressivity of the current personal
19 income tax portion. But what we haven't discussed --
20 and there's a lot of caution about this -- because of
21 the difficulty with precision, passing judgment on the
22 incidence of the BNRT in particular. But, nevertheless,
23 I think we need to have before this Commission a
24 discussion of that. That needs to happen.

25 Second, it seems to me that we need to --

1 COMMISSIONER EDLEY: "Safety valve."

2 CHAIR PARSKY: -- make sure that there is a more
3 detailed description of what I think is properly referred
4 to as a "safety valve."

5 I think there is unanimous -- there is
6 considerable Commission concern about the unintended
7 consequences of the package as described. And one
8 suggestion that I think is worth having work done, is
9 how could we create a specific safety valve --

10 TELEPHONIC VOICE: *"Pardon the interruption.*
11 *Your conference contains less than three participants at*
12 *this time."*

13 CHAIR PARSKY: Okay. Are all of you not
14 listening?

15 Okay, I'm joking, I'm joking.

16 And the suggestion made is that something along
17 the lines of at the end of Year Three, having had three
18 years of transition from 2012 through 2014, when there
19 still is left and in place a relatively low BNRT rate,
20 and still at least -- and we may want to refine this a
21 little bit -- still left, at least 2 percent of the sales
22 and use tax left to be reduced, that we would think about
23 designating a group of tax experts within the combination
24 of the Department of Finance and the Franchise Tax Board,
25 we'll come up with something --

1 COMMISSIONER BOSKIN: Including outside people?

2 CHAIR PARSKY: It might include outside people,
3 but we'll suggest something -- and I'd welcome any
4 thoughts along that line -- that would determine the
5 sales tax would be proposed to be reduced and the BNRT
6 increased, unless this group determined that the
7 anticipated revenue was not there and, therefore, the
8 sales tax potential should not be reduced as designed.
9 Something along those lines. And I would welcome input
10 over the course of the next few days on that.

11 But we need to come back with a mechanism for a
12 safety valve in case our anticipation doesn't bear fruit.

13 And then people should step back and assess the
14 nature of the recommendation that is being made for the
15 package as a whole. And I want to come back to the
16 elements that are still on the table. But with respect
17 to the package that would include -- that potentially
18 would include a business net-receipts tax, I draw
19 everyone's attention to the memo that John and Chris
20 wrote -- and I'll just read the paragraph:

21 *"We are confident that the tax package is the*
22 *right course for California. We also recognize that the*
23 *BNRT represents an extraordinary change in California's*
24 *tax code. A tax change of this magnitude should only*
25 *occur after the proposal has been fully vetted and all*

1 *of the ramifications fully assessed by the Legislature*
2 *and the Governor and the public. We believe" -- and*
3 *this could be the Commission -- "We believe that the BNRT*
4 *is sufficiently promising to warrant the Commission's*
5 *recommendation that the Legislature and the Governor*
6 *proceed with a public process to fully evaluate the BNRT*
7 *proposal, and upon satisfactory completion of the*
8 *process, to enact the BNRT into law as part of the*
9 *proposed package."*

10 Something along those lines would introduce any
11 recommendation that would include the package; but that
12 what I'd like you to think about, the Commission would
13 still be seeking, at the end of that process, a vote on
14 the package as a whole.

15 I think that may offer a way for an appropriate
16 level of sensitivity to the magnitude of this suggestion,
17 the magnitude of the reform.

18 Now, in addition, between now and Monday, we
19 still have to decide how the proposal, outlined by Fred
20 Keeley and the proposal outlined by Michael Boskin -- or
21 proposals -- fit in. Should they be -- is it a sense of
22 this Commission that they should be included in Section 1,
23 or should they be, if enough Commission concurrence
24 doesn't occur, should they be included in Section 3?

25 COMMISSIONER POMP: Do you mean to include a

1 severance tax proposal as well?

2 COMMISSIONER LOZANO: I only heard -- I heard
3 initially it had to do with the progressivity and the
4 lower income, which is a comment on something already
5 before us.

6 CHAIR PARSKY: Right, right.

7 COMMISSIONER LOZANO: The only real proposal
8 is on the offshore drilling and the royalties.

9 CHAIR PARSKY: Yes, I think Michael was clearly
10 making the point that his support, if you will, for the
11 proposition that's on the table is in question because
12 it doesn't include a minimum tax. And so --

13 COMMISSIONER BOSKIN: I'm not the only
14 commissioner in that situation.

15 CHAIR PARSKY: And so commissioners need to
16 think about that, as to whether or not, in the spirit
17 of compromise, they can support the proposal without it.

18 But in addition to that, the proposal on
19 additional offshore oil and the proposal with respect to
20 a pollution tax, needs to be considered. A severance
21 tax, as suggested, was not part of the tax package, but
22 could be part of Section 3.

23 COMMISSIONER POMP: Michael's is part of the
24 tax package?

25 CHAIR PARSKY: Yes.

1 COMMISSIONER BOSKIN: Yes.

2 COMMISSIONER POMP: When was that?

3 CHAIR PARSKY: If you look at the two-page --

4 COMMISSIONER BOSKIN: For several meetings now.

5 CHAIR PARSKY: For several meetings and that
6 I distributed by e-mail three times -- three times. It
7 is contained in that.

8 COMMISSIONER EDLEY: Okay, but that's not to
9 say that -- I guess what I was hoping is that there would
10 be an opportunity for people to -- I mean, without
11 getting into Robert's Rules or anything -- that there
12 would be an opportunity for people to propose adding or
13 deleting something from a core set that we know there's
14 strong consensus around. So, for example, it seems to me
15 that there is not --

16 COMMISSIONER BOSKIN: I think what you mean is,
17 refining the core package, is that -- more or less. I
18 mean, several people have raised the purpose. Did you
19 want to refine the core package; is that what you're
20 talking about? Or do you want to add a new thing in it?

21 COMMISSIONER EDLEY: Well, I think I mean
22 refinement.

23 CHAIR PARSKY: Correct. I certainly would think
24 that.

25 COMMISSIONER EDLEY: I mean, look, let me just

1 be candid. Let me be candid. I think that -- and maybe
2 this is best left to sort of some one-on-one discussions.
3 But I think that we -- at some point, I think we need to
4 have at least an informal show of hands or something to
5 see whether or not there is sufficient support -- if you
6 want to include -- Michael's thing about the minimum tax
7 was not included in the motion that John and I made.

8 CHAIR PARSKY: And was not included in a
9 recitation of the tax package.

10 COMMISSIONER EDLEY: Okay.

11 CHAIR PARSKY: That's why I interpreted it as
12 raising concerns about his support for --

13 COMMISSIONER BOSKIN: It's also -- it, like
14 your refundable thing, is a refinement of the tax --

15 COMMISSIONER EDLEY: That should be considered,
16 and we ought to see whether or not there are the votes
17 for it. That's right.

18 With respect -- and I agree with it.

19 Then with respect to the drilling, et cetera --
20 I have to get smarter -- this is off the record
21 because --

22 CHAIR PARSKY: Did you hear that up there?

23 COMMISSIONER EDLEY: -- I'm supposed to be a
24 law school professor who once taught tax. I've got to be
25 smarter on the relative merits of the severance tax

1 versus royalty tax, and also I'd like to have a
2 conversation about whether Michael's proposal could be
3 amended so that he's not changing environmental policy,
4 but merely setting up, if you will, a standby tax, so
5 that if at some point there is additional drilling on
6 state or federal lands, then this is the tax rate that
7 would exist. It would already be there, it wouldn't
8 require a new two-thirds vote, but it would already be
9 there. So it would be a standby tax that would be
10 created, should the State's policies with respect to
11 drilling would otherwise change. That sounds to me
12 pretty good. And I'd be very interested in considering
13 that as part of Track 1. And we could talk about what
14 would happen with the revenue, should that ever be --
15 should that ever eventuate.

16 As to whether it's a royalty or a severance,
17 I am agnostic, and would just like these two guys to arm
18 wrestle and tell us which one --

19 COMMISSIONER POMP: Just consider mine a
20 refinement of Michael's, that's all.

21 CHAIR PARSKY: Yes, that's fine. If seen in
22 the context of a refinement of Michael's proposal, we'll
23 take them up one at a time. That seems appropriate.

24 COMMISSIONER EDLEY: But then let me just --
25 since I'm on a roll here, let me suggest --

1 CHAIR PARSKY: You're doing great.

2 COMMISSIONER EDLEY: The reason that -- I would
3 like a little clarity -- for us to all have a little bit
4 of clarity on the Curt-versus-Fred issue, for the
5 following reason is. I think that if --

6 CHAIR PARSKY: They've been going at it for
7 years. For years.

8 COMMISSIONER EDLEY: But so, for example, if we
9 could have something along the line that Curt suggests,
10 that essentially tries to hold constant the public policy
11 goal of Prop. 42 in the way that Curt suggested, doing
12 violence to the rest of our package only in the sense
13 that it creates a carve-out from what would otherwise be
14 flowing into the general revenues, I again personally
15 would be supportive of that as being part of the package.

16 But then to the extent that that happens, then
17 I think what remains of Fred's policy goals needs to be
18 framed in a clear-enough way that it could be considered,
19 at least for purposes of Track 3. And I thought kind of
20 signaling that now would at least allow Fred and others
21 who are like-minded to do the work between now and Monday
22 to actually shape that -- to shape that.

23 Does that make any sense? Do you see what I
24 mean?

25 In other words, I don't want to be in a

1 situation --

2 COMMISSIONER KEELEY: I'm not clear.

3 COMMISSIONER EDLEY: I don't want to be in a
4 situation on Monday in which your full proposal gets shot
5 down, so to speak. I think that's the technical term.
6 I haven't served in the Legislature, but...

7 COMMISSIONER KEELEY: That's the term. That's
8 the polite term.

9 CHAIR PARSKY: Not at the Commission, only at
10 the Legislature.

11 COMMISSIONER EDLEY: And we're in a situation
12 in which Fred's full proposal gets shot down. Curt's
13 proposal gets accepted and there is no opportunity for us
14 to consider the missing piece of Fred's proposal in the
15 context of a --

16 CHAIR PARSKY: I think the way --

17 COMMISSIONER BOSKIN: I think the intention has
18 been that if things that have been on the table don't
19 survive "1," they will be considered in "3."

20 CHAIR PARSKY: Absolutely.

21 COMMISSIONER BOSKIN: They may or may not
22 survive.

23 CHAIR PARSKY: Absolutely.

24 COMMISSIONER BOSKIN: And maybe some people
25 won't vote for "1," if their thing isn't in "3."

1 CHAIR PARSKY: No, I think that is true. But
2 I think that's exactly right. I would -

3 COMMISSIONER KEELEY: Mr. Chairman, I thought
4 that --

5 COMMISSIONER COGAN: You wanted clarity. You
6 wanted clarity on the proposal.

7 CHAIR PARSKY: I was interpreting, Fred, that
8 your proposal would stay intact, and it will be considered
9 by the Commission, a first, as part of Section 1.

10 COMMISSIONER KEELEY: Okay.

11 CHAIR PARSKY: If enough support for that
12 proposal doesn't exist, then it will be considered as
13 part of Section 3 as a whole.

14 COMMISSIONER KEELEY: Okay, now, let me ask a
15 question about that. I'm not sure I have a big
16 disagreement with that, but it depends on the answer to
17 the next couple of questions.

18 So let me ask you to think about this,
19 Mr. Parsky --

20 CHAIR PARSKY: "Gerry."

21 COMMISSIONER KEELEY: There are -- oh, you're
22 not going to take me down that path.

23 CHAIR PARSKY: Bob Hertzberg said to take you
24 down that path.

25 COMMISSIONER KEELEY: To take me down that path.

1 There are aspects of the core package that
2 three commissioners have been working on that are very
3 hard for me to choke down. So let me be specific.

4 I think, for example, that what is being
5 proposed relative to the personal income tax is, in my
6 judgment, not the best policy foot that we could put
7 forward.

8 I think that I like the way that you have
9 feathered together -- the three of you have feathered
10 together very nicely, I think, the idea of stepping
11 across the adoption and implementation of a BNRT. I
12 think it's varied, I think it's conservative, meaning
13 careful and thoughtful. Whether it's a good idea, I like
14 this idea of creating a safety valve and so on.

15 The bank and corporation tax component, I'm a
16 little lost on why it even is a good idea to do that, to
17 zero that out. It's \$10 billion in the general fund.
18 I understand you can shift most of those folks over. I'm
19 still unclear on what the impact is on the bank and
20 financial services sector who, in my judgment, have,
21 shall we say, we don't have any problem in California
22 attracting the bank and financial services sector into
23 the state of California. So there is no reason to create
24 any economic incentives, in my judgment, for them to come
25 here. They're already here. They're going to continue

1 to do business here. We're the sixth, eighth, tenth
2 largest economy in the world. They're going to be here.
3 So I don't understand that. But I'm willing to do a lot
4 of stretching on this.

5 But let me try to do this this way: I am very
6 appreciative and deeply respect the work that the three
7 of you have done. It is the work that the three of you
8 have done with the full knowledge and participation of a
9 lot of other commissioners and a lot of people in the
10 public. And you've put a good package on the table. I
11 don't agree with all of it.

12 The PIT is particularly troubling to me. The
13 idea that we are going to -- however you slice it and cut
14 it, the fact of the matter is, the PIT will provide, the
15 way it is structured, this reduction will provide a very
16 big tax relief for the wealthiest people in California,
17 in my judgment. It will provide some benefit to all PIT
18 payers, but it will provide the biggest benefit to those
19 who need it the least in my judgment. That's my judgment
20 about it.

21 So I'm not taken with that.

22 I could be convinced that as part of the package
23 that included this tax that I have advanced, that has
24 been -- you and I agreed there would only be one workshop
25 entity, and it would be focused on what you folks did.

1 But you and I talked about the opportunity to have a
2 working group. And so we had a very public process, and
3 it involved a lot of people, it had the same structure
4 you had, in the sense of having a pre-meeting and two
5 very public meetings, developing a written report a week
6 and a half ago, plus legislation. I feel like we played
7 by the rules and submitted things in good faith.

8 The idea that it's now either in Bucket 1, if
9 there's sufficient support, or Bucket 3 if not, I'm okay
10 with that, provided we can have that conversation about
11 all aspects of the package then.

12 CHAIR PARSKY: We should.

13 COMMISSIONER KEELEY: And I'm not trying to be
14 argumentative.

15 I'm saying, I have trouble with the PIT. So
16 if that pertains to everything in the package, then I'm
17 okay with it pertaining to the thing that I'm in love
18 with. And I think that's just simple fairness around
19 here.

20 COMMISSIONER PRINGLE: You're not supposed to
21 fall in love with your bills.

22 COMMISSIONER KEELEY: I know. That's why I had
23 to leave the Legislature, because I kept falling in love
24 with my bills.

25 That's the first thing they tell you in the

1 Legislature: Don't fall in love with your bills. The
2 second thing is, don't talk when a microphone is on.

3 But some people only paid attention to the first
4 rule and not the second one, apparently.

5 Yes, kick them while they're down.

6 So if there's a way, Gerry --

7 CHAIR PARSKY: Where's Hertzberg? He's around
8 here somewhere.

9 COMMISSIONER KEELEY: If you just would think
10 about which, because if you're asking, frankly, some of
11 the more progressive folks on the Commission to stretch,
12 to go here with something that, on the PIT -- I understand
13 how it's being -- how the sizzle was being put out there,
14 but there is also a reality of what's being proposed on
15 the PIT. I might be able to choke that regressivity down
16 if we are doing something on this excise tax, which I
17 think -- I mean, unless somebody tells me I'm wrong on
18 this, I think we've made a pretty compelling case how
19 this fits every single one of the Governor's objectives,
20 every single one that he outlined.

21 And if we're going to then debate where is the
22 tax neutrality, then everybody should be at risk who has
23 proposed something here.

24 And so I'm willing -- you know that I'm willing
25 to stretch and try to find a way to make it work and all

1 of that. I would just say, please don't single the
2 excise tax out as sort of: Well, if you can get the
3 support for it, we'll put it in Bucket 1, otherwise, it
4 goes in "3." I think we need a little more mixing to test
5 the veracity -- or not the veracity, I'm sorry, that's the
6 wrong word -- strike that. No, because that's not what
7 I meant.

8 COMMISSIONER EDLEY: I understand what you
9 meant.

10 COMMISSIONER KEELEY: I didn't mean honesty.
11 I meant, the viability politically here at the Commission
12 of the other ideas, too.

13 CHAIR PARSKY: I think your point is very well
14 taken. And I'd like the commissioners to think about,
15 over the weekend, how compromise can be reached. For
16 some, it may mean that the package can be supported as is,
17 with these refinements, as long as it includes the excise
18 tax. For others, it might mean, well, they could support
19 it as long as it includes the royalty or severance tax.

20 So I think we need to think about the package
21 that is still on the -- the only thing we've taken off
22 the table is the split roll, because when people -- that
23 no one supported.

24 But you're right, I was trying to outline,
25 certainly, some further work that needs to happen, that

1 needs clarification on this safety-valve concept and the
2 distribution impact. But I didn't mean to suggest we
3 treat one thing one way and the other part of the package
4 another. They will be viewed the same.

5 COMMISSIONER KEELEY: Thank you, Mr. Chairman.

6 CHAIR PARSKY: Michael.

7 COMMISSIONER BOSKIN: I'd like to make one quick
8 comment for my colleagues on the panel that Fred has
9 described as progressives. I use that as a scientific
10 description, not as an epithet. And I respect that point
11 of view.

12 And I just want to make it clear, since there
13 seems to be this notion that somehow progressives are
14 getting shortchanged in this, let me tell you what
15 conservatives are -- again, a scientific description --
16 are being asked to do.

17 Let me just --

18 COMMISSIONER PRINGLE: No, no.

19 COMMISSIONER BOSKIN: Let me just make this
20 comment. I don't mean to give --

21 COMMISSIONER BARRALES: Do we have to go over it
22 to get your point?

23 COMMISSIONER BOSKIN: No, but I'm just saying,
24 we're adding -- first of all, we're creating a new tax
25 with a very broad base, that everywhere else in the world

1 has been used to grow government substantially. We're
2 being asked to remove millions of Californians
3 contributing to the general fund --

4 CHAIR PARSKY: Why do you think he supported it?

5 COMMISSIONER BOSKIN: -- and we're adding a
6 large number of non-C-corp businesses as tax collectors
7 and, to some extent, taxpayers, among many other things.
8 So I think the proper way to view this is, there are lots
9 of puts and takes. Each of us are going to have to decide
10 whether we can support this whether --

11 CHAIR PARSKY: That's true.

12 COMMISSIONER BOSKIN: I mean, I'm being asked --
13 I'm giving a lot even to get near the package that's
14 being discussed, to be honest, okay. I'm keeping an open
15 mind and, you know, I've gone a long way on a lot of my
16 principles.

17 Maybe Becky and I are the only ones that feel
18 strongly about a minimum tax, et cetera. I don't know
19 what they are.

20 But I'm just saying, you have to be aware that
21 on the other side, people have given a lot already to get
22 to this area, as have people on your side have given to
23 get to this area, and Chris and John are doing a fabulous
24 job in trying to work it out.

25 Whether in the end we'll all be able, or the

1 vast bulk of us in both parties will be able to support a
2 package remains to be seen. I hope it's the case. I
3 certainly have been working towards that and have been
4 trying to do it. But I just don't want to leave the
5 impression that it's only the people that describe
6 themselves as liberal Democrats or as progressives that
7 are having a hard time with any of this, because the
8 conservatives are being asked to give up a lot to do this
9 in the name of getting some improvement in volatility and
10 incentives, and so on. You're getting a lot out of this
11 as well as giving, as are we.

12 COMMISSIONER PRINGLE: Mr. Chairman, I'd like
13 to figure out how I could give today as opposed to give on
14 Monday. And that is -- and I know how much I've given.
15 And, actually, the package that we've seen has spent the
16 last three months fleshing it out, understanding it
17 better, talking about phasing. And, you know, there are
18 people that like that, people that don't like the package.

19 And I like the package that was presented by
20 Mr. Edley and Mr. Cogan. I think there's ways to enhance
21 it and make it better, such as the review period and
22 other elements. The issue regarding the gas tax that I
23 suggested, it doesn't need to be in the first phase, even
24 though I think it would probably be smart because it
25 would necessarily reduce the BNRT amount, which I hope

1 that we could cap at 4 percent.

2 But my challenge is, as you know, I'm not going
3 to be here Monday, and I want to ensure there's a
4 mechanism by which I can record the things I support and
5 I won't list the things I oppose because it takes support
6 to get something accomplished. So I'd like to figure out
7 what mechanism by which we could establish that today.

8 So I, for one -- and I don't know anybody
9 else's travel plans, I just know my wife's, and I have
10 to be with her.

11 CHAIR PARSKY: I wouldn't suggest otherwise.
12 I've talked to your wife extensively. She's not prepared
13 to go alone.

14 Let me come back and say, I also wanted to say
15 that Ruben arranged a call with a number of business
16 interests that were very concerned about the package that
17 is being suggested. It kind of further illustrates that
18 there are a series of potential compromises that are going
19 on here. And I revert back to Fred's comment about
20 compromise without compromising your principles.

21 And the only thing I would say is that, at a
22 time when most Californians think Sacramento -- rightly or
23 wrongly, but Sacramento is dysfunctional --

24 COMMISSIONER KEELEY: Rightly.

25 CHAIR PARSKY: -- that no one seems to be able

1 to compromise, all I would say to commissioners between
2 now and September 20th, is to think about the notion that
3 if, as broad a cross section of different points of view
4 as are represented around this table, can find a way to
5 reach concurrence and compromise, it will send an
6 incredible signal to Sacramento that basically says,
7 "This is what the people really want you to be doing."
8 So I just would bear that in mind.

9 In terms of the process, I am very concerned
10 at making sure every single commissioner has the ability
11 to express his or her views in the report. In the report.
12 And there is a little bit of an issue about commissioners
13 that will not be here, or potentially can't be here on
14 Monday -- be at Berkeley on Monday, and may not either --
15 and even if they were on the phone, how that would work.
16 So I want to think a little bit more about this and
17 consult with counsel.

18 But my thought was -- is -- that we will see
19 on Monday if, as close to unanimity around the table as
20 possible, without, quote, formally voting, can be
21 achieved. And if it can, the draft recommendation
22 section will be prepared. And each commissioner would
23 be asked, after reading it, to either sign the report or
24 not sign the report. It's up to them. And therefore
25 every single commissioner would be able to express his or

1 her view on the recommendations without violating any
2 issues of the public law or any of that.

3 But I would not be comfortable if we had four
4 commissioners -- and I tried, believe me, I have tried
5 every single day between now and September 20, including
6 the weekends, to see if we could get every commissioner
7 in the room; that wasn't achievable. I think this would
8 clearly at least satisfy me from the fact that every
9 commissioner was as respected as every other one in their
10 views.

11 And I've had an opportunity to talk to every
12 single commissioner. I want to continue that discussion,
13 to make sure that there is a full understanding of each
14 commissioner's view in that regard. But that would be my
15 suggestion of how to get to a point of issuing a report.

16 COMMISSIONER POMP: So, let me see if I
17 understand. So if you can't get unanimity, there will be
18 a report, and then people will sign on or not?

19 CHAIR PARSKY: Well, I'm hoping that coming up
20 on Monday there is a consensus without a vote around the
21 table of those who are there, that will permit the staff
22 to draft a report reflecting that view. Those people --
23 and presumably, the people in the room -- would say "Yes."
24 I mean, we will have an opportunity to see if the words
25 reflect the consensus.

1 But the commissioners that are not there or who
2 are on the phone and not in a public place, will still be
3 given an opportunity not to sign that report if it doesn't
4 reflect their views.

5 COMMISSIONER POMP: And will be given a chance
6 to explain why.

7 CHAIR PARSKY: You are always given a chance to
8 explain why.

9 COMMISSIONER POMP: The question is, whether it
10 will be incorporated into the report.

11 CHAIR PARSKY: Richard, I anticipate that your
12 letter supporting the report can be included, as all of
13 your comments have been included. If that's what you are
14 looking for, we'll ask the Commission if they would think
15 that that's appropriate.

16 But I would like to try to avoid, if we could,
17 because of the message we're trying to send to Sacramento,
18 I'd like to avoid having to reflect a vote with a minority
19 group named. If we can't avoid it, we can't avoid it.

20 COMMISSIONER PRINGLE: Mr. Chairman, first off,
21 there will be the main package in Section 1, as you
22 suggested; correct?

23 CHAIR PARSKY: Right.

24 COMMISSIONER PRINGLE: And your drive is to
25 get the maximum number of members, if not unanimity or

1 consensus, or whatever other words you used. I would like
2 to suggest that there should not be a minority report
3 offered on Section 1. I mean, that is --

4 CHAIR PARSKY: Well, I put Section 2 with it
5 because Section 2 is the rainy-day fund, and so those two
6 sections are linked.

7 COMMISSIONER PRINGLE: Right. I mean, the point
8 is, if the people that do not choose to sign it, the lack
9 of their support is the lack of their support.

10 I think what we do is, I also would extend it
11 to Section 3. I mean, I believe that people would
12 have -- maybe you're seeking a majority of the people on
13 this board to recommend items for Section 3. I think if
14 every other member outside that majority -- let's say
15 there's 14 members here, that means if eight voted for
16 Mr. Keeley's plan, I don't think it's appropriate to have
17 then six letters of why they think Mr. Keeley's plan is
18 bad included in the report.

19 I mean, the way you have partitioned it is to
20 say, this is the overwhelming majority on Sections 1 and
21 2, and that's why they're here, and the signatures
22 represent those people who support it. Section 3 will
23 be other proposals that may have just a simple majority
24 of this body, and an articulation as to why that simple
25 majority feels that's important, and their signatures

1 will represent that, too.

2 I think if we start allowing for contrary
3 submissions, what you'll do is you'll fill the whole
4 report up with objections, and you'll have more
5 objections than --

6 COMMISSIONER BOSKIN: I have a very much
7 simpler view of Section 3. I think the action is going to
8 be around Sections 1 and 2 because of the rainy-day fund.

9 CHAIR PARSKY: Right.

10 COMMISSIONER BOSKIN: There are some very
11 strongly held views about some other things. I think if
12 there is some modest support, we can decide if that is
13 eight or five -- or more than one person, obviously,
14 whatever that number is -- you can just have a section
15 that said, "Here are a variety of proposals that some
16 commissioners thought were very important and worthy of
17 consideration by the Governor or Legislature that neither
18 commanded overwhelming support to be included in
19 Section 1. And even if there are people opposing them,
20 let some commissioners oppose, and then just have them
21 in there. You don't have to have everybody sign every
22 individual thing. That's silly.

23 CHAIR PARSKY: I kind of feel something like
24 that.

25 COMMISSIONER BOSKIN: I think a process like

1 that rather than trying to avoid having days of wrangling
2 about the wording of some --

3 COMMISSIONER PRINGLE: And, Dr. Boskin, you're
4 talking about your point just in Section 3, though, where
5 there may be a collection, more than one and possibly
6 less than a majority, that say these are other ideas of
7 Commission members.

8 COMMISSIONER BOSKIN: That's right.

9 COMMISSIONER PRINGLE: So it's not portraying
10 that the Commission is supporting that position, that's
11 what I --

12 COMMISSIONER BOSKIN: Right, that's the idea.
13 No one would -- therefore, no member of the Commission
14 who either didn't support it or strongly opposed it would
15 be portrayed as having supported it. And there would just
16 be a list of things in there that we had worked on, that
17 some commissioners supported, did not commend -- that we
18 think that some commissioners think should be commended
19 for consideration by the Governor and Legislature, that
20 did not rise to the level of substantial-enough support to
21 be included. And, indeed, there were some commissioners
22 who opposed them, that's all. And then there would just
23 be a list. And at least those questions would be raised
24 without any need to have like a Supreme Court opinion,
25 where every single subsection had, 6-to-3 on this thing,

1 but 5-to-4 on that, and 7-to-2 on that.

2 No disrespect.

3 COMMISSIONER EDLEY: Jeez.

4 COMMISSIONER BOSKIN: I know they will all be
5 9-0, when you're the chief justice.

6 COMMISSIONER LOZANO: Yes, I just want to --
7 I also don't want to register votes. I think that the
8 package should go forward with a significant or
9 substantial majority, and it should reflect that.

10 I would be -- I don't think we should have
11 minority opinions or opposing opinions. I think the body
12 has had enough opportunity to deliberate. They were on
13 the record if we're not supportive of certain aspects of
14 this.

15 I am concerned about this Section 3 now.
16 Because what I thought we had originally said is that,
17 yes, if ideas have come forward that don't fit in "1" or
18 "2" that reflect a -- I don't know -- it's not consensus,
19 and it's certainly not the majority -- but if there are
20 opinions that are --

21 COMMISSIONER BOSKIN: There needs to be a
22 minimum. There needs to be a minimum number of people.

23 COMMISSIONER LOZANO: But there has to be a
24 minimum.

25 COMMISSIONER BOSKIN: It can't be just one

1 person or a couple.

2 COMMISSIONER LOZANO: It can't be one or two.
3 That's what I think.

4 COMMISSIONER BOSKIN: It has to be several.

5 COMMISSIONER EDLEY: May I make a proposal, sir?

6 CHAIR PARSKY: Well, I made one, which I didn't
7 get too much response for.

8 COMMISSIONER EDLEY: Right, so can I try an
9 alternative.

10 COMMISSIONER PRINGLE: Define the number of
11 people.

12 COMMISSIONER EDLEY: Right. That's what I'd
13 like to do.

14 COMMISSIONER LOZANO: 30 percent. I would say
15 five -- four or five, something like that. 30 percent.

16 COMMISSIONER EDLEY: What I would suggest is
17 that -- look, two things: With respect to Section 3,
18 I would prefer that these be ideas where all of us are
19 saying, even if we disagree with it, this is a serious
20 idea and we really think the Legislature ought to mull it
21 over.

22 COMMISSIONER BOSKIN: Even if we disagree with
23 it.

24 COMMISSIONER EDLEY: This deserves to be on
25 the --

1 COMMISSIONER BOSKIN: I'm unlikely to vote for
2 Fred's proposal, but it's a serious proposal.

3 COMMISSIONER EDLEY: And so with that in mind,
4 then what I would suggest for Part 3, is that a proposal
5 goes in Section 3 if it has five votes or more, of which
6 at least one must be of the other party.

7 COMMISSIONER KEELEY: The other appointees?

8 COMMISSIONER EDLEY: Of the other party.

9 COMMISSIONER LOZANO: Of the other appointees?

10 COMMISSIONER KEELEY: You mean appointees?

11 COMMISSIONER LOZANO: Yes, appointees.

12 COMMISSIONER KEELEY: A Governor's appointee and
13 the Legislative appointee.

14 COMMISSIONER EDLEY: Whatever, yes. Fine, fine.

15 CHAIR PARSKY: There's no party representative.

16 COMMISSIONER EDLEY: Oh, yes. Okay, yes, I
17 forgot excuse me. So, yes, thank you -- no, no.

18 COMMISSIONER COGAN: Yes, yes. You mean "yes."

19 COMMISSIONER EDLEY: I do? Okay, I do.

20 Okay, so that would be my first suggestion.

21 But the second is, the second idea --

22 COMMISSIONER PRINGLE: Actually, I like that.
23 That's good.

24 COMMISSIONER EDLEY: But then the other thing
25 I would say, I have to say -- maybe this is the academic

1 in me, but I'm really uncomfortable with anything that
2 even has the appearance of gagging people who have
3 invested all this time in this thing and have a point of
4 view, have a concern, even if it's an isolated one.

5 And what I would suggest for those is they
6 simply be in an appendix, and that they are not in Part 3
7 but they be in an appendix. In essence, what we're doing
8 is we are lending the Commission's publishing capacity to
9 let folks who have views; and then I would just try to
10 prevail upon everybody in the spirit of the enterprise,
11 not to take advantage of that in order to undermine the
12 collective effort.

13 But I guess I just don't --

14 COMMISSIONER PRINGLE: Who is the editor of the
15 spirit for the enterprise?

16 COMMISSIONER EDLEY: The individual. The
17 individual. And I --

18 COMMISSIONER PRINGLE: Really?

19 COMMISSIONER BOSKIN: We're looking for Captain
20 Kirk somewhere, I think.

21 CHAIR PARSKY: Well, why don't we think about
22 this a little bit?

23 I would just urge everyone to think about the
24 notion that -- a couple of things: Think about the fact
25 that the report will have maximum effect and command

1 serious consideration if it includes all of the
2 commissioners.

3 I think that the voice to those that just can't
4 agree with the compromised package is expressed by not
5 signing on to the report.

6 COMMISSIONER KEELEY: Mr. Chairman?

7 CHAIR PARSKY: But I do think -- again, and I
8 have made this suggestion for people to think about --
9 that less than a majority of commissioners should permit
10 something to be in Section 3.

11 I had requested -- reminded all Commissioners --
12 by e-mail, that if you had items to be included
13 potentially in Section 3, please provide them to the
14 staff in descriptive form, I think we said by August 24th.
15 And I will tell you that there were not a long array of
16 full descriptions to be included in Section 3.

17 Now, I don't want to quell anyone's verbosity,
18 but --

19 COMMISSIONER EDLEY: Creativity, you mean.
20 Creativity.

21 CHAIR PARSKY: Or creativity. But most all of
22 what would potentially be included in Section 3 have been
23 discussed today. There is nothing floating around there.

24 And the only question really is, and I do think
25 a measure of whether it should be included is, do enough

1 commissioners think it's worthy of serious consideration
2 by others than the Commission.

3 COMMISSIONER BOSKIN: Even if they oppose it?

4 COMMISSIONER EDLEY: Yes, exactly.

5 CHAIR PARSKY: Yes.

6 COMMISSIONER KEELEY: Mr. Chairman, if I might?

7 CHAIR PARSKY: Yes.

8 COMMISSIONER KEELEY: Thank you, Mr. Chairman.

9 First, there's an evolution going on here, and
10 that's why we meet, is to have our thinking evolve both
11 in form and in substance. And I think there's an
12 evolution going on here now in terms of form of the
13 report. My recollection is that, I thought what you
14 sent out by e-mail defining what would be in the three
15 categories, I sent you back an e-mail about -- there was
16 literally a one-word change that I was interested in you
17 making. But I thought you captured it well there, that
18 essentially the first category were those things that
19 could be enacted by the Legislature and the Governor, and
20 no further action was needed. So that means limited to
21 statute.

22 Number 2 --

23 CHAIR PARSKY: And revenue-related.

24 COMMISSIONER KEELEY: Yes. Oh, yes, yes,
25 absolutely.

1 And Bucket 2 were those things that the
2 Legislature and the Governor could not enact on their own.
3 For example, constitutional amendments that need to be
4 ratified by the voters.

5 And then Bucket 3, as I recall, were those
6 items that had come to our attention, which neither were
7 in A or B, but would be good for the fiscal soundness of
8 the State, and that you were seeking --

9 CHAIR PARSKY: For others to consider.

10 COMMISSIONER KEELEY: -- for others to consider.
11 And that's -- for example, and I then stimulated
12 California Forward, that Mr. Hauck and I are on, to submit
13 their 10-point package for inclusion in Number 3.

14 So it sounds like maybe that one's changing a
15 little bit, Bucket 3, a little bit.

16 Here's something I'd ask literally for you to
17 think about, because I don't think this is the time for
18 us to make it easier on each other to get Buckets 1 and 2
19 figured out. I think this is the time to make it hard
20 on us to do that. I think this is the time where, rather
21 than saying, "Don't worry about it. You'll get your thing
22 in Number 3, somehow it will be in the report and don't
23 worry about it," you didn't say that.

24 CHAIR PARSKY: No.

25 COMMISSIONER KEELEY: I'm just saying, I don't

1 think we should relieve ourselves of any pressure at this
2 point. I think you should push us harder to get to this
3 consensus.

4 This is the real hard work, today and Monday is
5 the real hard work for us, where we're going to see --
6 we're not hearing from others. You know, we finished that
7 stuff, the input is over. We're now seeing, what can we
8 do together.

9 CHAIR PARSKY: Agreed.

10 COMMISSIONER KEELEY: Where can we stretch with
11 each other?

12 And I'm trying to send as loud and clear a
13 signal as I can, I'm willing to take the very good work
14 that you've done; and even though I have principled
15 disagreements on the PIT, I am willing to go there if
16 what happens is that -- and this is the give and take we
17 should all engage in -- I think that this fuels tax,
18 pollution tax, green fee, whatever we want to call it,
19 I think it's a very meritorious proposal that fits
20 absolutely into the charge that we were given by the
21 Governor.

22 And again, so what goes in Bucket 1 is really
23 critical. It's met the highest standards of the
24 Commission, it's had to, you know, run through a gauntlet,
25 it's had to change if people wanted it to change.

1 There's all kinds of things that are going to have to
2 happen. And I would ask you to put more pressure on us
3 to get to an agreement, not less.

4 CHAIR PARSKY: I will do everything I can over
5 the next few days to do just that.

6 Okay. We definitely will have a meeting. We
7 will also have the ability, under the guidelines, to talk
8 about for anyone who can't be at the meeting to plug in
9 by phone, and we will treat the voting issue the way I
10 described so that that doesn't do any injustice to
11 individual commissioners who can't be there.

12 And I just want to ask -- Curt, did you have
13 something? You're poised, I know.

14 COMMISSIONER PRINGLE: Yes -- no, I did, because
15 I don't want you to close down. One, I am not going to be
16 in a place where I can answer a phone on Monday --

17 CHAIR PARSKY: Okay.

18 COMMISSIONER PRINGLE: -- or to spend eight
19 hours on it.

20 CHAIR PARSKY: It will take us exactly one hour.

21 COMMISSIONER PRINGLE: All I want to do, though,
22 is just state now however the number of tallies that we
23 need to get, I do -- I've spent time with Dr. Boskin, I do
24 support his concept of some minimal personal income tax,
25 if it's referenced that way. I also support his offshore

1 oil, find all the money you can, even though it grows the
2 state budget. I'm not all excited about it, but I do
3 enjoy that concept.

4 And as I stated before, I support the proposal
5 as presented by Dr. Edley and Mr. Cogan on the package.

6 So I just wanted to make sure you know where
7 I'm coming from. And I would certainly like to look at
8 the other ideas as they are presented, possibly in greater
9 detail within the package. But that's -- if you want to
10 tally up where those things are, that's where I'm at.

11 CHAIR PARSKY: Thank you. I really appreciate
12 you saying that, Curt.

13 COMMISSIONER POMP: Let me just add, I am not in
14 a place where I can call on Monday, either.

15 And let me reinforce what Chris said. I don't
16 think you want to be viewed as having stifled dissent.
17 I think we have an obligation to the Legislature, as well
18 as other legislatures around the country who are going to
19 be watching this, to encourage a candid and open exchange
20 of views. And that would mean explaining, should it come
21 to that -- I hope it doesn't -- but should it come to
22 that, explaining why people felt they just couldn't go
23 along, so...

24 CHAIR PARSKY: All I would ask is that -- and
25 I know this may be semantics -- I would ask that you

1 refrain from pointing directions at me. I'm not making
2 any decisions for the Commission. I'm trying to get the
3 commissioners to decide what it is they would like to do.

4 So we'll come to a conclusion in terms of how
5 the report should be structured as a commission, as we
6 have come to everything.

7 Okay, Monica?

8 COMMISSIONER LOZANO: Well, I'm not I'm going
9 to be there, either, on Monday. So let me just generally
10 say --

11 CHAIR PARSKY: I'm only talking to you, have no
12 fear.

13 COMMISSIONER LOZANO: Yes, I know we will talk,
14 and so --

15 COMMISSIONER EDLEY: Where are you guys all
16 going?

17 CHAIR PARSKY: Well, there's a group going,
18 they're going to Cancun.

19 COMMISSIONER POMP: Can we get on that cruise
20 ship?

21 COMMISSIONER EDLEY: I want to be on that
22 commission.

23 COMMISSIONER LOZANO: Anyway, I'm generally
24 supportive, and I want to thank all the work. I think
25 Package 1 is really a very strong step forward.

1 I am not inclined at this moment to support
2 the inclusion of a minimum tax for all Californians. I
3 am also not inclined to support the other proposal on
4 the offshore drilling revenues only because I don't know
5 enough. And so if we can get more information about how
6 that would work and whether or not it's an extension of
7 what currently is in place in terms of -- so that I just
8 need more information.

9 I would want us to articulate a ceiling on the
10 business net-receipts tax. I'm concerned about the rate
11 and the way it works in tandem, so I'd encourage you to
12 do that. And I'm also very appreciate of what you're
13 going to do in terms of analyzing the entire package as
14 it relates to progressivity. So I want to get that back
15 to us.

16 And everything else, without going through my
17 long list of notes, I think we've been very consistent
18 with the ideals. I think we've worked with the
19 small-business community to help identify what their
20 concerns are.

21 Fred, I like your proposal. And I especially
22 like it as it relates to the sales tax and how those two
23 will play off of each other.

24 I'm concerned about it actually becoming an
25 additional tax burden. And I want to better understand

1 how that works. So just right now, I'm feeling generally
2 fairly supportive of that well.

3 CHAIR PARSKY: Thank you very much for those
4 views.

5 I just want to ask, are there any members of
6 the public that are still here -- there's a method to my
7 madness here but -- yes, sir?

8 MR. SPILLANE: I'm one.

9 CHAIR PARSKY: Go right ahead.

10 MR. SPILLANE: I thought you were taking --

11 CHAIR PARSKY: I'm trying to see if there's
12 anyone that would like to speak.

13 MR. SPILLANE: Yes, sir.

14 CHAIR PARSKY: Go ahead.

15 MR. SPILLANE: Okay.

16 COMMISSIONER EDLEY: A couple of us have to
17 leave for planes. Can we get at least some reassurance --
18 I really want to make sure that those of us who have to
19 leave get the benefit of at least a digest of what the
20 public comments are going to be?

21 CHAIR PARSKY: Yes.

22 COMMISSIONER EDLEY: Because these folks have
23 waited all day.

24 CHAIR PARSKY: No, no, and I'm prepared to stay
25 with them without any question. We'll make sure that

1 there's a record of what they submitted.

2 COMMISSIONER DE LA ROSA: Before we go, though,
3 do you think we're just going to meet for four hours?

4 CHAIR PARSKY: I am very anxious --

5 COMMISSIONER DE LA ROSA: I'm happy to stay
6 later.

7 CHAIR PARSKY: No, no, no, I'm very anxious to,
8 on Monday, stick to our time frame. I'm going to try to
9 talk individually to everyone, to see what can be done to
10 advance that, but I didn't anticipate that this would end
11 on time because of the discussion we're on. But I think
12 we're getting close to knowing whether or not it's
13 something that can be supported or not.

14 COMMISSIONER DE LA ROSA: That's great. Just a
15 point of information.

16 CHAIR PARSKY: Yes, sir. And I know you've made
17 comments at several of our meetings, but please go ahead.
18 I'd like to limit it to a minute, if it's all right.

19 MR. SPILLANE: Seven hours' wait for the minute.
20 Thank you, sir.

21 My name is Bill Spillane, and I'm with Americans
22 for Fair Taxation.

23 I've given you two hard copies and one
24 electronic copy of the solution to what you're talking
25 about.

1 Two issues: Number one, any income tax is
2 highly volatile. When a person loses their job, the tax
3 revenue from that person goes to zero. However, he still
4 eats and he still pays his rent or whatever. So if you
5 use a sales tax in lieu of an income tax, you won't have
6 such an unstable revenue source in California. That's a
7 huge solution.

8 Now, then, regarding the BNRT, that's a great
9 way to lose jobs for California, that's a great way to
10 discourage investment in California because you're
11 going to be adding a price increment on top of
12 California-produced prices. And our high-value producers
13 want to export not only within the states, but abroad.
14 And this is not WTO-compliant. You will not be able to,
15 quote, border-adjust it, rip that tax out in order to
16 export broadly in the world, and they'll be uncompetitive.

17 Do you want uncompetitive business here in
18 California? Of course, not. You want to encourage
19 business. You want to encourage investment. So you need
20 to not tax business because they're a source of jobs and
21 revenue. The BNRT does that nicely, but it's something
22 that's added to the prices. That's very counterproductive
23 and makes all of our businesses uncompetitive worldwide
24 and U.S.A.-wide.

25 Follow the examples of Texas and Florida. It's

1 not complicated.

2 Please read the letter again, all the solutions
3 are in here. It does justice to the Governor's goals,
4 every single one of them. And if the goals are simply not
5 to be given lip service, this is the solution, a simple
6 sales tax.

7 And, by the way, on page six, you'll see that,
8 with a rebate, it's progressive. There's the scale of
9 the progressiveness of this tax with a pre-bate, which is
10 a rebate of taxes in advance to the people that need it.
11 That's very simple.

12 That's all I have to say.

13 Thank you very much.

14 CHAIR PARSKY: You're welcome.

15 Next, could you just introduce yourself?
16 Because I have a whole list here but I'm not sure.

17 MR. KHOURI: Absolutely, sir.

18 Thank you, Mr. Chair, Members. Gus Khouri on
19 behalf of the California Transit Association. I'll be
20 very brief.

21 I appreciate the hard work that the Commission's
22 put in.

23 Just very briefly on the pollution tax, the
24 sales tax, and transit needs in general.

25 With respect to the sales tax, let's start with

1 that first. As far as the impact, if you lower the sales
2 tax, it would impact Proposition 42, the sales tax on
3 gasoline; the sales tax on diesel, which goes to transit;
4 the sales tax on the back 9¢ through the 1990 gas tax
5 increase of the excise tax; as well as the spillover
6 mechanism that Mr. Genest spoke about earlier. So that's
7 all basically the base funding for public transportation
8 in the state.

9 As you all know, it's been well-documented,
10 funding for public transportation has been virtually
11 eviscerated on the state level. Operations funding has
12 been eliminated until at least the 2012-2013 fiscal year.
13 So that makes our job that much more difficult in trying
14 to comply with the state's mandates of reducing greenhouse
15 gas emissions, with yourselves as part of the solution.

16 Yes, we have received money through
17 Proposition 1B and through the federal stimulus package.
18 That is for capital expenditures. So we actually need
19 the money to be able to operate the trains and the buses.
20 And as you see here in Los Angeles at six o'clock in the
21 evening, as you will see shortly, congestion is horrible.
22 So we're trying to move people that much more efficiently,
23 we're trying to reduce traffic congestion, move the
24 elderly, school children that much more efficient.
25 There's absolutely no way that we're going to be able to

1 raise \$200 billion over the short-term. As you saw, it
2 was a difficult effort just to generate \$20 billion
3 through Proposition 1B in 2006.

4 So transit operations, if nothing else, that you
5 hear me say is definitely of the greatest importance.

6 With respect to Mr. Keeley's proposal, I very
7 much appreciate the efforts, sir, that you're trying to.
8 I very much appreciate the collaboration that you've
9 engaged the association in.

10 We would like to see transit capital be
11 addressed as some of the proposed expenditures.
12 Specifically, with respect to the SB 375 components.

13 So thank you very much. I appreciate
14 everybody's time. And I look forward to working with the
15 commission.

16 CHAIR PARSKY: Thank you very much.

17 MR. SHAW: Thank you, Mr. Chairman and Members
18 of the Commission. I will be brief as well, as I have
19 spoken on a couple of occasions before.

20 I do wonder if my agreeing with Mr. Keeley --

21 COMMISSIONER KEELEY: State your name.

22 MR. SHAW: Michael Shaw, at the National
23 Federation of Independent Business.

24 I do wonder if my agreeing with Mr. Keeley on a
25 number of things today is a sign of how long this meeting

1 has gone, or --

2 COMMISSIONER KEELEY: You've lost your mind.

3 CHAIR PARSKY: But here are a lot of people that
4 agree with Mr. Keeley.

5 MR. SHAW: Yes, there are, and very, very smart
6 people as well.

7 CHAIR PARSKY: About football teams, baseball
8 teams.

9 COMMISSIONER KEELEY: That's right.

10 MR. SHAW: Excuse me, I wanted to mention a few
11 things as you consider putting together this proposal for
12 consideration next week.

13 We do find, as representing small businesses,
14 the disparity in eliminating the corporate tax while
15 preserving the personal income tax. And I know that
16 there's discussion about how this all works out in the
17 wash. And, obviously, those numbers we have yet to see
18 to fully understand. And we are willing to reconsider
19 how we feel about this. However, on the face of it, it
20 seems very disparate treatment. Because, first, small
21 businesses, 80 percent file in the personal income-tax
22 system. So when you add to that the business net-receipts
23 tax, for the personal income tax filers, and you only have
24 the business net-receipts tax on the corporate side, that
25 seems unfair treatment.

1 We would also recommend that the thresholds
2 mentioned in the draft proposals be indexed. Because as
3 we've seen in other states such as Michigan, that has
4 come back to bite them in the rear, so to speak, on a
5 number of occasions, both with the single business tax
6 that they had previously, as well as the current Michigan
7 business tax. They don't have indexing of their
8 thresholds.

9 The business and net receipts phase-in sales
10 tax phaseout kind of formula is something that is of
11 concern, obviously not knowing what the rates will be.
12 We do appreciate the Commission's discussion on that
13 today with regard to reviews and finding ways to balance
14 that as well.

15 I do have one additional concern with regard
16 to all these changes of conformity with federal law.
17 Because as we move more towards the value-added tax or
18 business net-receipts tax and we can argue whether or not
19 those are similar in principle, but it is moving away
20 from federal law in terms of the conformity with our
21 income tax system we have today. And so that is something
22 that we do need to consider. Because while the state
23 component may become more simple and easier to comply with
24 as a result of these proposals, which I think is
25 questionable as well, it does complicate the state-federal

1 relationship. So for a small business filing their taxes
2 at the federal level, they're now going to have to redo
3 all these calculations, and that's going to change things
4 for them as well. Now, we'll add more time and commit a
5 higher cost for them.

6 I wanted to thank you for the time as well and
7 for the excellent staff work of Mr. Ibele and the rest of
8 the members.

9 CHAIR PARSKY: Thank you all very much.

10 I think with that, our meeting is concluded.

11 Thank you all very much.

12 *(The meeting concluded at 6:00 p.m.)*

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REPORTER'S CERTIFICATE

I hereby certify:

That the foregoing proceedings were duly reported by me at the time and place herein specified; and

That the proceedings were reported by me, a duly certified shorthand reporter and a disinterested person, and was thereafter transcribed into typewriting; and

That the foregoing transcript is a record of the statements of all parties made at the time of the proceeding.

IN WITNESS WHEREOF, I have hereunto set my hand on the 13th day of September 2009.

DANIEL P. FELDHAUS
California CSR #6949
Registered Diplomate Reporter
Certified Realtime Reporter